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reported; memorandum opinions denying motions for new trial and for reargument (R. 675–680) are reported in 138 F. Supp. 138. The opinions on application for interlocutory injunction (R. 601–639) are reported at 134 F. Supp. 132. The opinions denying a stay pending appeal (R. 639–642) are not reported. The opinion of Mr. Justice Harlan granting a partial stay (R. 643–650) is reported in 75 Sup. Ct. 912.

The reports of Division 4 (R. 414–446) and of the full Commission (R. 506–515) in the merger proceedings are reported in 290 I. C. C. 725 and 295 I. C. C. 11, respectively. The opinion of Division 4 in the preferred stock exchange (R. 518–537) is not reported.

JURISDICTION

The judgment of the district court was entered on December 23, 1955 (R. 555–557), and motions for a new trial and for reargument (R. 675–680) were denied on January 27, 1956. Notices of appeal were filed by the various appellants in No. 36 on January 31, 1956 (R. 3–22), February 1, 1956 (R. 22–24), and February 3, 1956 (R. 30–31); in No. 82 on February 23, 1956 (R. 24–30); and in No. 114 on March 26, 1956 (R. 1–2). Probable jurisdiction was noted in No. 36 on April 23, 1956 (R. 681), and in Nos. 82 and 114 on October 8, 1956 (R. 682).

STATUTES INVOLVED

Pertinent provisions of the Interstate Commerce Act and the Investment Company Act of 1940 are set forth in the Appendix, *infra*, pp. 45–52.

QUESTIONS PRESENTED

1. The basic issue before the Court is whether the Interstate Commerce Commission had jurisdiction over the Alleghany Corporation for the purpose of approving a new preferred stock issue by Alleghany. In this connection, the United States will discuss the following questions:

a. Whether the ICC erred in holding that Alleghany, a non-carrier which indirectly controlled a subsidiary carrier in the New York Central Railroad Company system through its direct control of Central, "acquired control" (under Section 5 (2) of the Interstate Commerce Act) of such subsidiary as a result of the latter's merger with another carrier in the Central system.

b. If not, whether an earlier ICC order subjecting Alleghany to carrier status was operative at the time of the stock order.

2. We shall also discuss briefly the following additional questions:

a. Whether the ICC orders which the court below set aside are subject to judicial review.

b. If so, whether the plaintiffs (minority common stockholders of Alleghany) had standing to bring the action.

c. Whether, in view of the recent decision of the Securities and Exchange Commission denying an exemption from the Investment Company Act of 1940 for Alleghany's new preferred stock issue, the district court's injunction against consummation of such issue should be vacated as no longer necessary.

STATEMENT

These are consolidated appeals from the judgment of a three-judge district court, convened under 28 U. S. C. 2321–2325 and 2284, which set aside two orders of the Interstate Commerce Commission ("ICC") and enjoined the consummation of a new preferred stock issue by Alleghany Corporation ("Alleghany") authorized by the second of the two orders. We shall here merely state such facts as are necessary to a consideration of the issues discussed in this brief (*supra*, p. 3).

THE ADMINISTRATIVE PROCEEDINGS

In November, 1940, Alleghany registered with the Securities and Exchange Commission ("SEC") as an investment company under the Investment Company Act of 1940, 15 U. S. C. 80a–1 *et seq.* (R. 185, 193). In 1944 Alleghany and the Chesapeake & Ohio Railway Company ("C & O") jointly filed with the ICC an application under Section 5 (2) of the Interstate Commerce Act [1] for approval, *inter alia*, of Alleghany's prior acquisition of control of C & O as well as two

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[1] Section 5 (2) (a) (i) provides:

"It shall be lawful, with the approval and authorization of the Commission, as provided in subdivision (b)—

"for two or more carriers to consolidate or merge their properties or franchises, or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership; or

"for any carrier, or two or more carriers jointly, to purchase, lease or contract to operate the properties, or any part thereof, of another; or

"for any carrier, or two or more carriers jointly, to acquire

other carriers, the Nickel Plate and the Pere Marquette (R. 418). On June 5, 1945, the ICC granted the application. *Chesapeake & O. Ry Co.* Purchase, 261 I. C. C. 239. The order of approval further provided, under Section 5 (3) of the Act,[2] that Alleghany ("unless and until otherwise ordered by the Commission") was to be considered a "carrier" subject to the provisions of Sections 20 (1)–(10) and 20a (2)–(11), which deal with issues of securities, reports, accounts, etc. (R. 185).

Section 3 (c) (9) of the Investment Company Act of 1940 provides that a company "subject to regulation under the Interstate Commerce Act" shall not be

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control of another through ownership of its stock or otherwise; or

"for a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise; or

"for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise; * * *"

[2] Section 5 (3) provides in pertinent part:

"(3) *Non-carrier deemed carrier upon acquiring control.* Whenever a person which is not a carrier is authorized by an order entered under paragraph (2) of this section, to acquire control of any carrier or of two or more carriers, such person thereafter shall, to the extent provided by the Commission in such order, be considered as a carrier subject to such of the following provisions as are applicable to any carrier involved in such acquisition of control: Sections 20 (1)–(10), 304 (a) (1) and (2), 320 and 913 of this title (which relate to reports, accounts, and so forth, of carriers), and sections 20a (2)–(11), and 314 of this title (which relate to issues of securities and assumptions of liability of carriers), including in each case the penalties applicable in the case of violations of such provisions."

deemed an investment company. After the ICC had subjected Alleghany to regulation as a carrier, the SEC on October 4, 1945, ordered that Alleghany's registration under the Investment Company Act should cease to be in effect (R. 185–186). The order provided that, "if in the future Alleghany Corporation ceases to be subject to regulation under the Interstate Commerce Act," the order "may be revoked, suspended or modified after appropriate notice and opportunity for hearing" (R. 186).

On January 19, 1954, Alleghany sold its C & O stock (R. 186–187). Prior thereto, its Nickel Plate stock had been sold, and the Pere Marquette line had been merged with the C & O (R. 614). On May 26, 1954, Alleghany prevailed in a proxy contest for control of New York Central, and elected its slate of directors to Central's board (R. 417, 513).

On June 22, 1954, on being advised by Alleghany's counsel of Alleghany's divestiture of control over C & O, the ICC ordered Alleghany to show cause why the ICC should not vacate the 1945 order and thus terminate Alleghany's carrier status (R. 188–189). Alleghany responded that it had no objection to entry "at a proper time" of an order terminating its authority to control C & O, but it requested the ICC to withhold action pending the filing of an application involving the lease and merger of two Central subsidiaries. According to Alleghany, the grant of that application would permit the continuance of Alleghany's carrier status (R. 189). The ICC postponed action on its show cause order for 60 days (R. 189–190).

Subsequently, on September 17, 1954, Alleghany, Central and two subsidiaries of the latter (the Louisville and Jeffersonville Bridge and Railroad Company, and the Big Four Railroad) filed a joint application under Section 5 (2) of the Act for ICC approval of the merger of the Bridge Company into the Big Four, and the lease of the Bridge Company's properties by the Big Four to Central (R. 210–233, 248–250). Central owned 98.98% of the Big Four's common stock, and 86.45% of its preferred stock; the Big Four owned all the common stock of the Bridge Company (R. 217, 417–418). Alleghany, alleging that it controlled Central, the Big Four, and the Bridge Company (R. 217), and that under the rule of *United States* v. *Marshall Transport Co.*, 322 U. S. 31 (see *infra*, pp. 26, 28–29) it was therefore a necessary party to the proceedings (R. 230), requested the ICC to continue its carrier status (R. 233).

On March 2, 1955, Division 4 approved the proposed merger as being in the public interest (R. 414–446). Its order also provided that Alleghany should be considered as a carrier for purposes of Sections 20 and 20a (R. 447), and that the "effective portions" of the prior status order of June 5, 1945, were "terminated" and had "no further force and effect" (R. 447).[3] On

[3] Division 4 stated (R. 424) that without a further ICC order Alleghany's divesting itself of its control of C & O "could not operate to alter the status of Alleghany as a carrier subject to the Act."

May 24, 1955, the full Commission affirmed (R. 506–517).[4]

On February 18, 1955 Alleghany filed with the ICC an application for authority to issue a new class of 6% convertible stock to be offered in voluntary exchange for its outstanding 5-½% preferred stock (R. 371–392). The stated purpose of this exchange, which had been approved at a meeting of Alleghany shareholders on February 8, 1955 (R. 372), was to eliminate approximately $18,000,000 of dividend arrearages on the 5-½% preferred (R. 385–386). On May 26, 1955, Division 4 approved (with a minor modification) the stock issuance (R. 518–536), and on June 22, 1955, the full Commission denied reconsideration (R. 554).

THE PROCEEDINGS IN THE DISTRICT COURT

The instant action, filed on June 6, 1955 by Alleghany minority common stockholders, was brought to set aside the ICC order of May 24 subjecting Alleghany to carrier status (R. 32–53).[5] The complaint was

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[4] On March 22, 1955, Division 4 approved an application by Alleghany and Central to acquire control of the Boston and Albany Railroad Company and two railroads which connected with the latter and whose properties were leased to it (R. 450–473). Central operated the Boston and Albany under a lease, but owned none of its capital stock (R. 454). The Commission noted (R. 453) that, in connection with its approval of the Bridge Company merger, it had recently provided that Alleghany should continue to be considered as a carrier; its order in the *Boston and Albany* case did not provide for such carrier status (R. 471–473). See *infra*, note 25.

[5] The plaintiffs, however, made no challenge of the ICC's approval of the merger, in itself, of the Bridge Company into the Big Four.

filed subsequent to the order by Division 4 approving the preferred stock issuance, but prior to the full Commission's affirmance thereof. A supplemental complaint challenging the preferred stock orders was subsequently filed (R. 93–101, 112–116, 557–560).

The complaint sought a preliminary injunction (R. 38), and on June 15, 1955, the district court issued an order to show cause why such injunction should not issue, returnable on June 23 (R. 53). On the latter date, Alleghany learned that the full Commission had affirmed the preferred stock order on the preceding day, and immediately began distribution of the new stock pursuant to the exchange offer (R. 604). Such distribution was halted by a temporary restraining order issued late that day by the district court (R. 56), after approximately 900,000 of the 1,300,000 shares of the proposed issue had been distributed (R. 647–648).

After hearing, the district court (District Judges Dimock and Walsh; Circuit Judge Hincks dissenting) granted an interlocutory injunction which prohibited Alleghany from taking any action pursuant to the ICC's orders or from issuing, distributing, transferring, or converting into common stock any of the new preferred stock (R. 102–107).[6] The injunction, insofar as it related to the 900,000 shares of preferred stock already issued, was stayed by Mr. Justice

[6] In a lengthy opinion (R. 601–628), the court, after reviewing the grounds upon which the plaintiffs challenged the Commission's orders (R. 613–627), held that the complaint raised "serious" issues, and that plaintiffs would suffer irreparable damage unless a stay issued (R. 627). Judge Hincks' dissent (R. 629–639) rested solely on his view that irreparable damage had not been shown.

Harlan pending appeal to this Court (R. 110–112, 643–650). On final hearing, the district court (Circuit Judge Frank sitting in place of Judge Hincks because of the latter's illness, R. 652) held unanimously that the injunction should be made permanent (R. 651–673). The court's final judgment (R. 555–557) set aside the order in the merger proceedings (except insofar as it authorized the merger itself and Central's control and lease of the merged properties) and the order authorizing the preferred stock exchange, and enjoined Alleghany and its agents or employees from "taking any steps in connection with or in furtherance of the issuance" of the new preferred stock, "or the transfer thereof" (R. 556).

In its final opinion, the court reaffirmed its holding that the ICC had erred in subjecting Alleghany to carrier status and in subsequently approving the preferred stock issue.[7] The court pointed out (R. 652–653) that, in the case of a non-carrier already in control of a carrier, the provisions of Section 5 (3) of the Act do not come into play until the non-carrier undertakes under Section 5 (2) "to acquire control" of another carrier. It reasoned (R. 653–654) that, since Alleghany (assuming *arguendo* that it controlled Central at the time of the merger, as Alleghany contends) already had control of the merged company

[7] The court stated (R. 652) that it adhered "for the most part" to what was said previously in the majority opinion granting the temporary injunction. The court also adhered (R. 660–661) to its prior rulings (R. 606–613) that the orders were reviewable and that the plaintiffs had standing to maintain the action.

(through its control of Central), so much of the Commission's order as purported to authorize Alleghany "to acquire control" thereof was a "legal nullity" (R. 654). In the court's view of Section 5 (2) (R. 653–654), a non-carrier in control of a carrier does not "acquire control" of another carrier through a merger transaction unless the non-carrier, by reason of the merger, acquires control of a carrier which it did not already have. In an appendix (R. 664–669), the court discussed the pertinent ICC decisions on the question whether intrasystem rearrangements constitute an acquisition of control, and concluded that "the Commission's interpretations have been not at all consistent and uniform" (R. 654).[8]

The court rejected the contention that Alleghany still had carrier status by virtue of the 1945 order (R. 655–660). It ruled (R. 655–657) that the 1945 order was no longer in effect when the Commission

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[8] In an appendix to its opinion (R. 670–673), the district court set forth several alternative grounds for reversing the Commission's orders. These grounds would be reached only if this Court were to hold that under Section 5 (2) Alleghany "acquired control" of the Bridge Company through the merger (R. 663). The district court stated (R. 670) that the ICC determination that Alleghany controlled Central "cannot stand" because (*a*) the findings as to such control are insufficient, (*b*) the evidence does not support them, and (*c*) the ICC erred in denying the plaintiffs' request for an evidentiary hearing on the issue of control. The court also stated (R. 672) that "The ICC opinions were further defective in their failure to find that the acquisition by Alleghany of control of the Central was consistent with the public interest." The court concluded (R. 670) that, if it were wrong in holding that the ICC had no jurisdiction, the case should be remanded to determine (1) whether Alleghany controls Central and (2) whether such control is in the public interest.

authorized the merger, since it "became inoperative" early in 1954 when Alleghany divested itself of control of C & O. The court further held (R. 657) that, in any event, the Commission had expressly terminated the 1945 order in the merger proceedings, so that when it subsequently approved the preferred stock issue, the 1945 order was no longer in effect.

The court concluded (R. 657) that, since Alleghany was not within ICC jurisdiction at the time of the preferred stock order, the issuance of the stock would violate the Investment Company Act. This conclusion rested on the court's view that the 1945 SEC order which terminated Alleghany's registration under the latter Act became inoperative "at the very latest" on May 24, 1955, when the ICC terminated its 1945 status order in connection with approving the merger, and that "Alleghany was then forthwith within the coverage of the Investment Company Act" (*ibid.*). In this connection, the court adhered (R. 661–662) to its earlier holding (R. 612–613) that injunctive relief was necessary to protect the common stockholders from the irreparable damage they might suffer if denied the protection of the Investment Company Act, namely, possible dilution of their equity through conversion of the new preferred stock.

THE SUBSEQUENT SEC PROCEEDINGS

On December 9, 1955 (three weeks after the district court's final opinion but before final judgment), Alleghany registered with the SEC under the Investment Company Act, stating that it was reserving the right to terminate such registration if this Court should determine that the ICC had correctly taken

jurisdiction over Alleghany. On February 24, 1956, Alleghany filed with the SEC an application for a determination that SEC approval was not required for the preferred stock exchange or, alternatively, for a retroactive exemption under Section 6 (c) of that Act from its provisions. On November 30, 1956, after hearing, the SEC (one Commissioner dissenting) denied the applications (Investment Company Act Release No. 2446).[9] The Commission held that the stock issue was not a senior security entitled to exemption under Section 18 (e), but rather a right to purchase prohibited by Section 18 (d). The SEC further held that the conversion feature of the new preferred stock made it so speculative that investors would have difficulty in determining its value, and that the Commission could not find, as it was required to do in order to grant an exemption, that the exchange was fair to the security holders affected and thus "in the interest of the investors".

SUMMARY OF ARGUMENT

I

A. The ICC order subjecting Alleghany to carrier status was reviewable. If, as Alleghany contends, the order had an immediate impact on business relationships, then it was directly reviewable. *Frozen Food Express* v. *United States*, 351 U. S. 40, 44. If, on the other hand, it was not directly reviewable because it lacked such impact, then it was reviewable in connection with review of the preferred stock order which rested upon it. Cf. *Pittsburgh Plate Glass Co.*

[9] The SEC's opinion is reproduced in full as an appendix to the SEC's *amicus* brief in this case.

v. *National Labor Relations Board,* 313 U. S. 146, 152.

B. The plaintiffs below, minority common stockholders of Alleghany, had standing to maintain the suit. While minority stockholders cannot challenge an ICC order if its only impact upon them is derivative through the corporation (*Pittsburgh & W. Va. Ry.* v. *United States,* 281 U. S. 479), they may challenge an ICC order when they have a "substantial financial or economic interest distinct from that of the corporation which is distinctly and adversely affected" by the order. *American Power & Light Co.* v. *Securities and Exchange Commission,* 325 U. S. 385, 388, 389. Alleghany's minority common stockholders had a "substantial financial and economic interest distinct from that of the corporation" in obtaining the protection of the Investment Company Act. Furthermore, their interest also was contrary to that of the preferred stockholders and the other common stockholders who had approved the exchange plan.

II

Section 5 (2) (a) (i) of the Interstate Commerce Act requires ICC approval, as "consistent with the public interest" (Section 5 (2) (b)), for any non-carrier which seeks "to acquire control" of two or more carriers or, if the non-carrier already controls one or more carriers, if it seeks "to acquire control" of another carrier. Section 5 (3) provides that when a non-carrier is thus authorized "to acquire control" of any carrier or carriers, it thereafter shall, "to the extent

provided by the Commission in such order, be considered as a carrier" subject to the applicable provisions of Sections 20 and 20a, dealing with security issues, reports, accounts, etc.

A. In *United States* v. *Marshall Transport Co.*, 322 U. S. 31, this Court held that where one carrier acquires the property and operating rights of another, a non-carrier which controls the acquiring carrier is a necessary party to the acquiring carrier's Section 5 (2) application, because the non-carrier indirectly "acquires control" of the acquired carrier. Since Alleghany is a non-carrier, the 1955 status order was ineffective to give the ICC jurisdiction over Alleghany unless Alleghany "acquired control" of the Bridge Company when the latter merged with the Big Four.

The ICC held that such an "acquisition of control" resulted from the merger because the resulting "rearrangement of the corporate structure of Central and its subsidiaries" constituted a significant modification of Alleghany's existing indirect control of the Bridge Company. We submit, however, that the merger affected neither the extent of Alleghany's control over the Bridge Company, nor the manner in which such control was exercised. Both before and after the merger, Alleghany controlled the Bridge Company indirectly through its control of Central. The only effect of the merger upon that control was to eliminate a corporate conduit through which it was exercised. The merger did not result in any further "acquisition" of control of the merged company by Alleghany.

The *Marshall* case, *supra,* relied on by the Commission to support its assumption of jurisdiction over Alleghany in the merger proceedings, is readily distinguishable. In *Marshall,* the non-carrier's subsidiary purchased the property and operating rights of another carrier with which it previously was not affiliated. In contrast, all that was involved here was an intrasystem corporate rearrangement which results in no material change in the non-carrier's indirect control of a carrier within the system.

The legislative history of Section 5 does not support the view that an intrasystem corporate rearrangement constitutes an "acquisition of control" by a non-carrier which already controls the system. It shows, we submit, that Congress intended to subject to ICC regulation only those "acquisitions of control" by a non-carrier which result in a combination of previously separate carriers under common control. The Bridge Company merger was not such an acquisition. The merging companies were already part of the integrated Central system, and the merger therefore did not result in combining under common control any carriers previously under separate management.

This construction of Section 5 (2) (a) (i) also accords with the purpose of Section 5 (3), which authorizes the ICC, in connection with approving an acquisition of control by a non-carrier, to subject to regulation certain of the latter's activities: issuance of securities, keeping of accounts, filing of reports, etc. As to all of these activities, there are sound reasons why regulation should be imposed (if at all)

when the non-carrier first brings the carrier under its control. Where the holding company already controls the subsidiary, however, there is no occasion for inaugurating such regulation merely because of an intrasystem corporate reshuffling.

B. The 1945 ICC status order did not give ICC jurisdiction to approve the preferred stock issue. That order provided that Alleghany would be considered as a carrier "unless and until otherwise ordered by this Commission * * *." On May 24, 1955, however, the ICC expressly "terminated" the 1945 order. Thus, when the ICC approved the preferred stock issue on June 22, 1955, the 1945 status order was no longer in effect.

III

The district court granted an injunction against consummation of the preferred stock exchange on the ground that it was necessary to protect Alleghany's common stockholders from injury they might suffer if denied the protection of the Investment Company Act. Since the injunction was issued, however, the SEC has denied an exemption from that Act for the preferred stock issue. In the face of that decision, we believe that consummation of the preferred stock issue by Alleghany would constitute a "willful" violation of the Investment Company Act.

Under Section 49 of that Act, such violations are subject to severe criminal penalties. We think that, if this Court affirms the decision of the district court, the threat of such penalties should suffice to deter Alleghany from attempting to consummate the ex-

change. Moreover, if the SEC should have reason to believe that Alleghany will disregard these criminal provisions, the SEC itself will have adequate opportunity to seek an appropriate injunction from the district court (under Sections 42 (e) and 44 of the Investment Company Act) during the 25-day period which customarily intervenes between the decision of this Court and issuance of the mandate.

Under these circumstances, we believe there is no occasion for this Court now to explore the power of a three-judge district court, convened under the Urgent Deficiencies Act, to enjoin threatened violations of the Investment Company Act. We therefore suggest that this Court may properly vacate the injunction without considering its initial validity.

ARGUMENT

INTRODUCTION

In the district court, the United States supported the ICC in defending its orders. However, upon further study of the issues and upon consideration of the court's opinions, the United States has concluded that the district court correctly held: (1) that Alleghany did not "acquire control" (under Section 5 (2) of the Interstate Commerce Act) of the Bridge Company through the merger of the latter with the Big Four, and that the ICC therefore had erred in subjecting Alleghany to carrier status;[10] and (2) that the 1945

[10] Throughout this brief, in the discussion of this issue, we will assume, as did the court below, that Alleghany has "control" over Central. We do not mean, however, to express any view as to the correctness of that assumption.

status order was terminated by this order in the merger proceedings.[11] Under this view, the ICC orders authorizing the preferred stock issue were invalid for lack of jurisdiction. Accordingly, we believe it unnecessary to consider the district court's several alternative grounds (set forth in an appendix to the district court's final opinion).

Two preliminary questions are also presented: (1) whether the ICC orders here involved are reviewable; and, if so, (2) whether the plaintiffs below had standing to seek such review. Prior to discussing (in Point II) the ICC's jurisdiction over Alleghany, we shall indicate briefly in Point I why we believe that the district court's affirmative answer to both preliminary questions was correct.

The appellants further argue that, even if the court below were correct in setting aside the Commission's orders, it had no power to enjoin consummation of the preferred stock exchange. This argument rests on the contention that a three-judge district court convened under the Urgent Deficiencies Act to review ICC orders has no authority to enjoin violations of the Investment Company Act. If the Court agrees with our views on the statutory issue, however, we believe that, in view of the recent SEC decision denying an exemption from the Investment Company Act

[11] For the reasons stated, *infra* (note 25), we also believe that the ICC's order in the *Boston & Albany* proceedings (see note 4, *supra*) was similarly ineffective to confer jurisdiction over Alleghany.

for Alleghany's preferred stock issue, it may now properly vacate the injunction without considering the difficult question of its initial validity.

I

THE ICC ORDERS WERE JUDICIALLY REVIEWABLE, AND THE PLAINTIFFS BELOW HAD STANDING TO OBTAIN SUCH REVIEW

A. THE ORDERS WERE REVIEWABLE

The district court held (R. 661) that, although the ICC order subjecting Alleghany to carrier status "by itself, may not have been reviewable, nevertheless, once the ICC made its order approving the issuance of the new preferred stock, there arose a right to seek review of the preferred stock order and also of the status order on which the preferred stock order was based." This conclusion, we submit, was clearly correct.[12]

It is well settled that certain types of administrative orders, not immediately reviewable, may infect with invalidity subsequent orders of the agency and that in such a case, upon judicial review of the later order, the earlier order will be reviewed so far as it may have affected the later order. See, *e. g., Algonquin Gas Transmission Co.* v. *Federal Power Commission*, 201 F. 2d 334, 337–338 (C. A. 1); cf. *United States* v. *Storer Broadcasting Co.*, 351 U. S. 192, 197. Thus, although an

[12] The ICC expressly disclaims any challenge to the reviewability of its orders (ICC brief, p. 74). Only Alleghany raises the issue.

order of the National Labor Relations Board certifying a particular group as a unit for collective bargaining purposes is not reviewable (*American Federation of Labor* v. *National Labor Relations Board*, 308 U. S. 401), its validity may be challenged as an incident to review of a finding of unfair labor practices based on an employer's refusal to bargain with such unit. *Pittsburgh Plate Glass Co.* v. *National Labor Relations Board*, 313 U. S. 146, 152. See also *United Air Lines* v. *Civil Aeronautics Board*, 228 F. 2d 13, 16 (C. A. D. C.).

Under these settled principles, we submit that the status order (assuming *arguendo* that it was not directly reviewable) was reviewable in connection with review of the preferred stock order. The latter plainly is reviewable, and Alleghany makes no contention to the contrary. Cf. *Schwabacher* v. *United States*, 334 U. S. 182. But if the preferred stock order is reviewable, so too is the status order since the preferred stock order depends directly on the status order. The Commission could validly authorize the preferred stock issue only if it had jurisdiction over Alleghany, and it had jurisdiction over Alleghany only if its status order were valid. In this respect, the two orders are inseparable for purposes of reviewability.

Alleghany's argument (Br. 35) that permitting judicial scrutiny of the status order in connection with review of the preferred stock order could lead to invalidation of "[c]ompleted transactions and business conduct pursued in good faith for many years in reliance upon the status determination * * *" proves too

much. For if the status order in fact results in such substantial changes in business relationships, then it would appear to have a sufficiently "immediate and practical impact" upon the parties affected to make it directly reviewable itself. *Frozen Food Express* v. *United States*, 351 U. S. 40, 44; *United States* v. *Storer Broadcasting Co.*, 351 U. S. 192, 198–200; cf. *Columbia Broadcasting System* v. *United States*, 316 U. S. 407, 421; *Rochester Telephone Corp.* v. *United States*, 307 U. S. 125.[13]

In sum, if the status order had the impact which Alleghany claims for it, then it was directly reviewable. If, on the other hand, it is not a "final" order, then its validity could be considered in connection with review of the subsequent order which rested upon it. Under either theory, it is reviewable.

B. PLAINTIFFS BELOW HAD STANDING TO MAINTAIN THE SUIT

Plaintiffs below, minority common stockholders of Alleghany, alleged in their complaint that the ICC orders deprived them (and other common stockholders) of their "rights, benefits, privileges and protections" under the Investment Company Act (R. 99; see R. 38), and threatened them with irreparable injury by possible dilution of their common stock

[13] In the *Rochester* case, a status order of the Federal Communications Commission, determining that a telephone company was subject to the Commission's regulatory jurisdiction and therefore was required to comply with a series of Commission orders, was held reviewable because it "necessarily and immediately carried direction of obedience to previously formulated mandatory orders addressed generally to all carriers amenable to the Commission's authority" (p. 144).

equity through conversion of the new preferred stock (R. 97–98). The district court held (R. 660, 661) that the plaintiffs had standing to seek review of the ICC orders, since the complaint alleged "threatened direct harm" to the individual stockholders, and that such individual injury was not converted "into an injury to the corporation which cannot be enforced except derivatively" merely because "all the common stockholders" were threatened with similar harm.

Alleghany argues (Br. 28–33, 35–38) that, since protection of the Investment Company Act is a right enjoyed by all stockholders collectively, minority stockholders have no standing to challenge an ICC order allegedly denying them that right. It relies primarily upon *Pittsburgh & W. Va. Ry.* v. *United States*, 281 U. S. 479, 487, where this Court held that minority stockholders in a railroad corporation had no standing to challenge an ICC order which allegedly threatened the financial stability of their corporation. The Court pointed out (p. 487–488) that "[t]he injury feared is the indirect harm which may result to every stockholder from harm to the corporation. Such stockholder's interest is clearly insufficient to give the Pittsburgh a standing independently to institute suit to annul this order."

However, in *American Power & Light Co.* v. *Securities and Exchange Commission*, 325 U. S. 385, 388, 389, this "accepted doctrine" was found inapplicable to a suit by "a stockholder having a substantial financial or economic interest distinct from that of the corporation which is directly and ad-

versely affected by an order of the Commission, irrespective of any effect the order may have on the corporation. * * *." There a holding company was held to have standing to challenge an order of the Securities and Exchange Commission which directed a wholly-owned subsidiary to make certain accounting entries which would result in removing from surplus certain moneys which otherwise would have been available for the payment of dividends to the holding company. The Court pointed out (p. 389) that, although the SEC order did not deprive the subsidiary of any asset or adversely affect the conduct of its business, it had "a direct adverse effect" upon the holding company as a stockholder entitled to dividends. The Court also held that one Okin, a minority common stockholder of Electric Bond & Share Company (a holding company which controlled American Power), had standing to challenge an SEC order approving a refinancing of an outstanding loan from Bond & Share to American Power. Okin challenged the refunding as illegal and fraudulent, and contended before the court of appeals that the refinancing "would reduce the value of his stock by reducing the interest income of Electric Bond and Share" (p. 387). The Court ruled (p. 392) that, since the corporation was "taking a position adverse to him" in seeking SEC approval of the refinancing, Okin had standing to maintain the suit.

In the instant case, Alleghany's minority common stockholders similarly had a "substantial financial and economic interest" in obtaining the protection of

the Investment Company Act which was "distinct from that of the corporation." Furthermore, Alleghany was "taking a position adverse" to its minority common stockholders by invoking ICC jurisdiction while the stockholders were challenging such jurisdiction and urging that the SEC was the proper agency to regulate Alleghany's security issues. Indeed, the interests of the minority stockholders were not only separate from those of the corporation, but also were contrary to those of the preferred stockholders and the other common stockholders who had approved the exchange plan. While Alleghany's common stockholders may have no general legal right "to have their equity in Alleghany maintained against dilution" (Alleghany Br. 37), they were entitled to protection against dilution resulting from invalid ICC orders, and therefore had standing to challenge such orders.[14]

II

THE ICC HAD NO JURISDICTION OVER ALLEGHANY WHEN IT APPROVED THE PREFERRED STOCK ISSUE

A. ALLEGHANY DID NOT "ACQUIRE CONTROL" OF THE BRIDGE COMPANY THROUGH THE LATTER'S MERGER WITH THE BIG FOUR

Section 5 (2) (a) (i) of the Interstate Commerce Act requires ICC approval, as "consistent with the

[14] Since Alleghany had invoked ICC jurisdiction, it presumably could not subsequently question it. Thus, the practical consequence of Alleghany's position that minority stockholders cannot challenge the assumption of jurisdiction over their corporation by the ICC would be to insulate such agency action from any judicial review, no matter how invalid it may be and regardless of its impact on interested parties.

public interest" (Section 5 (2) (b)), of certain mergers and related transactions. A carrier must obtain such approval "to acquire control" of another carrier and also to merge, purchase, lease, or contract to operate the properties of another carrier. Such approval must be obtained by a non-carrier, however, only when it seeks "to acquire control" of two or more carriers or, if the non-carrier already has control of one or more carriers, when it seeks "to acquire control" of another carrier. Section 5 (3) provides that when a non-carrier is thus authorized "to acquire control of any carrier or of two or more carriers, such [non-carrier] thereafter shall, to the extent provided by the Commission in such order, be considered as a carrier" subject to the certain provisions of the Act, including those dealing with security issues, reports, accounts, and similar matters.

In *United States* v. *Marshall Transport Co.*, 322 U. S. 31 (discussed *infra,* pp. 28–30), this Court held that, where one carrier acquires the property and operating rights of another, a non-carrier which controls the acquiring carrier is a necessary party to the acquiring carrier's Section 5 (2) (a) application, because in that situation the non-carrier indirectly "acquires control" of the acquired carrier. Since Alleghany is a non-carrier, the 1955 status order was ineffective to give the ICC jurisdiction over Alleghany unless Alleghany "acquired control" of the Bridge Company when the latter merged with the Big Four.

The ICC held (R. 514) that such an "acquisition of control" did result from the merger because the resulting "rearrangement of the corporate structure of Central and its subsidiaries" constituted a significant modification of Alleghany's existing indirect control of the Bridge Company. We submit, however, that the extent and form of Alleghany's control over the Bridge Company was not substantially changed by the merger; and that, in any event, the alleged change of control which resulted from the merger did not constitute the kind of non-carrier "acquisition of control" within the meaning of Sections 5 (2) and 5(3). Under either view, Alleghany did not "acquire control" of the Bridge Company through the merger.

1. Prior to the merger, the Bridge Company was a wholly-owned subsidiary of the Big Four. The latter, in turn, was an almost wholly-owned subsidiary of Central, and it was through the Big Four that Central controlled Bridge Company. Both before and after the merger, Alleghany's control of the Bridge Company was an indirect one that existed solely because of its control of Central.[15] The only effect of the merger upon Alleghany's control of the Bridge Company was to eliminate one corporate conduit through which that control was exercised. Whatever control Alleghany had of the Bridge Company was "acquired" when Alleghany obtained control of Central. The

[15] As pointed out *supra* (note 10), we assume *arguendo* that Alleghany possesses "control" over Central, as appellants contend.

subsequent merger of the Bridge Company with another carrier in the Central system which owned all of its stock did not affect either the extent of Alleghany's control over the Bridge Company or the manner in which such control was exercised. It did not constitute a further "acquisition" of control of the merged company by Alleghany.

United States v. *Marshall Tranport Co.*, 322 U. S. 31, relied on by the Commission (R. 514; see ICC Br. 29–30) and by Alleghany (Br. 62–63, 67–68) to support the Commission's assumption of jurisdiction over Alleghany in the merger proceedings, does not sustain the position that, under Section 5 (2) (a) (i), Alleghany "acquired control" of the Bridge Company through the merger. The facts in the *Marshall* case were as follows: Refiners Transport Terminal Company, a motor carrier, applied to the ICC for authority to purchase the property and operating rights of Marshall Transport Co., another motor carrier which it did not then control. The Commission denied the application on the ground that, since Union Tank Car Company (a non-carrier) controlled Refiners, the proposed purchase would result in Union's obtaining control of Marshall, and that Union therefore was a necessary party to the application in order to obtain Commission approval of such "acquisition of control."

This position was sustained by this Court, which held that Section 5 (2) required ICC approval, not only of the purchase of Marshall by Refiners, but also of "the acquisition of control of Marshall by

Union, through its control of Refiners" (p. 36). In reaching that conclusion, the Court pointed out (p. 38) that "the existence of control must be determined by a regard for the 'actualities' of intercorporate relationships," and it quoted with approval (p. 40) the Commission's statement that, unless the Act covered such indirect acquisitions of control, " 'a non-carrier holding company, or others, may expand at will without becoming subject to our jurisdiction' " by " '[p]roceeding thus through a controlled subsidiary.' "

In the *Marshall* case, the holding company did "acquire control" of Marshall as a result of Refiners' purchase, since such purchase brought Marshall under holding company control for the first time. But in the instant case, as we have shown, the " 'actualities' of intercorporate relationships" are that Alleghany already controlled Bridge Company before the merger, and that the merger did not change the extent of such control. From the fact, relied on by Alleghany (Br. 64–65), that Central may have "acquired control" of the Bridge Company through the merger, it does not follow that Central's parent similarly acquired control. For the effect of the merger was to convert Central's indirect control (through the Big Four) of the Bridge Company into direct control, whereas the merger made no material change in Alleghany's indirect control of the Bridge Company. See also *infra*, pp. 30–35.

Moreover, the policy reasons relied on in the *Marshall* case are absent here. In *Marshall*, the Court pointed out that, unless non-carrier indirect acquisi-

tions of control of hitherto independent carriers were covered by Section 5 (2), a non-carrier "may expand at will without being subject" to Commission regulation. But in the instant case the merger involved no "expansion" of Alleghany's operations to bring new carriers within its orbit; it was merely a corporate rearrangement within an integrated system which the non-carrier already controlled. See *infra*, pp. 30–35.

2. The legislative history of Section 5 does not support the view that such an intrasystem corporate rearrangement as the Bridge Company merger constitutes an "acquisition of control" by a non-carrier which already controls the system.[16] On the contrary, we believe that the history shows that Congress, in requiring ICC approval of an "acquisition of control" by a non-carrier, was using the term in its usual and ordinary sense—that is, to obtain control not previously possessed by the non-carrier.

Prior to the Transportation Act of 1920 (41 Stat. 481), Section 5 dealt only with the pooling of traffic and revenues, which it prohibited (24 Stat. 386).[17] In the 1920 legislation, Congress amended Section 5 to subject acquisitions of control by one carrier of another (which did not involve consolidation of such

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[16] The legislative history of Section 5 is set forth in detail in an appendix set forth in detail in an appendix to the ICC brief (pp. 84–110).

[17] Combinations of railroads were then dealt with under the antitrust laws. See, *e. g.*, *Northern Securities Company* v. *United States*, 193 U. S. 197; *United States* v. *Union Pacific Railroad Company*, 226 U. S. 61.

carriers into a single system) to ICC approval to determine whether they were in the public interest. Section 5 (4) directed the Commission to prepare a master plan for consolidation of the nation's railroads into a limited number of systems, and Section 5 (6) authorized the Commission to approve consolidations of carriers if they were in furtherance of such plan and would promote the public interest. However, Congress did not give the Commission any jurisdiction over acquisitions of carriers by non-carriers.

The latter omission proved a severe stumbling block to the Congressional policy of furthering consolidation of carriers pursuant to a nationwide plan. For, as the ICC pointed out to Congress in its annual reports, it soon became apparent that, through the device of the holding company, combinations of systems could be effected which stopped short of technical consolidation but which nevertheless would defeat any orderly plan for integration of the nation's railroads. See 43d I. C. C. Ann. Rep. 79–83 (1929). A lengthy Congressional investigation of railroad control and ownership followed, and the resulting report (H. Rep. No. 2789, 71 Cong., 3d sess., commonly known as the "Splawn Report" after its special counsel, Dr. Splawn) formed the basis for the Emergency Railroad Transportation Act of 1933 (48 Stat. 217–220). The provisions in Section 5 relating to acquisitions of control by non-carriers were introduced by that Act."

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[18] Section 5 was further amended by the Transportation Act of 1940 (54 Stat. 905). The amendments made no significant changes in the provisions here involved. They did, however, eliminate the

The Splawn Report rejected the suggestion that railroad holding companies should be prohibited (pp. XVII–XVIII). However, it recommended that Section 5 be amended "so as to bring within the jurisdiction of the Interstate Commerce Commission for approval or disapproval any acquisition of the control of a railroad which *would result in bringing that road into affiliation with, in control of, or under the management of another railroad,* whether the acquisition be by holding company or otherwise" (*id.*, p. LXXXV). (Emphasis added). Bills embodying that recommendation (H. R. 9059, 72d Cong., 1st Sess.; S. 844, 73d Cong., 1st Sess.) were drafted by Chairman Rayburn of the House Interstate & Foreign Commerce Committee, Commissioner Eastman, and Dr. Splawn. These bills (with exceptions not material here) were subsequently enacted as amendments to Section 5.

The purpose of the bills, as the legislative history shows, was to require ICC approval of "acquisitions of control" by a non-carrier only when they resulted in combining previously separate railroad properties under common control. Thus, Commissioner Eastman, whom this Court has described as "one of the weightiest voices before Congress on railroad matters" (*St. Joe Paper Co.* v. *Atlantic Coast Line R. Co.*, 347 U. S. 298, 304), stated that the bill was designed to eliminate an "important weakness" in Section 5,

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provision relating to formulation and implementation of the nationwide consolidation plan, apparently because "[b]y 1940 it had become apparent that the ambitious * * * plan of consolidation was not bearing fruit." *Schwabacher* v. *United States*, 334 U. S. 182, 193.

which (prior to amendment) "places no control on the activities of so-called holding companies *in effecting the unification of railway properties into systems*" (Hearings Before the House Committee on Interstate and Foreign Commerce on H. R. 9059, 72nd Cong., 1st Sess.). (Emphasis added). Commissioner Eastman pointed out that "these holding companies have been *bringing carriers under common control and hence combining them* without any supervision or approval by the Commission" (*id.*, p. 250). (Emphasis added). He stated that the bill was aimed at holding company activities "only insofar as they result in *accomplishing or effectuating control or management of two or more railroads in a common interest*" (*id.*, p. 61). (Emphasis added).[19] The testimony of Dr. Splawn was to the same effect (*id.*, pp. 278–279).

The Senate committee report on the bill explained that "the amendments of the consolidation provisions of the act give the Commission control over holding companies that acquire stock of railroads and *thereby effect consolidations* without approval of the Commission" (S. Rep. 87, 73d Cong., 1st Sess., p. 1); that there had been no opposition to the proposal that "holding companies should be under the control of the Commission *insofar as purchase of stock resulted in consolidation of railroad properties*" (p. 3); and that

[19] See also other portions of Commissioner Eastman's testimony at pp. 94–100 of the ICC brief. Thus, in response to the question "Is it not just as important if not more, that independent lines remain independent?", Commissioner Eastman answered: "Yes, that is my concern with respect to this bill. Not that holding companies tend to prevent consolidations, but that they bring about combinations of r roads without any public supervision whatsoever" (*id.*, p. 276

the "intent is to make impossible *the bringing of carriers under common control* through complicated schemes involving numerous interrelated holding companies * * *" (pp. 8–9). (Emphasis added in all three quotations). The same theme runs through the House report (H. Rep. No. 193, 73d Cong., 1st Sess.).

In sum, the legislative history shows, we believe, that the underlying purpose of Congress in providing for ICC approval of acquisitions of control by non-carriers was to correct the "important weakness" of Section 5 as it then stood, *i. e.*, that "it places no control upon the activities of so-called 'holding companies' *in* effecting *the unification of railway properties into systems*" (statement of Congressman Rayburn, manager of the bill in the House, 77 Cong. Rec. 4857). (Emphasis added). Therefore, when Section 5 speaks of "acquisitions of control" by a non-carrier, it refers only to those acquisitions whose result is to combine previously separate carriers under common control.

That test is certainly not satisfied here. Alleghany's "activities" in connection with the merger had nothing to do with "accomplishing or effectuating control or management of two or more railroads in a common interest," or "the bringing of carriers under common control," or "effecting the unification of railway properties into systems." The Bridge Company and the Big Four were already part of the integrated Central system at the time of the merger (R. 511–512). The merger, in fact, did not even result in any substantial tightening of Alleghany's

control over the subsidiary carriers.[20] See *supra*, pp. 27–28.

This construction of Section 5 (2) (a) (i) also accords with the apparent purpose of Section 5 (3). The latter section authorizes the ICC, in connection with approving an acquisition of control by a non-carrier, to subject to regulation certain of the latter's activities: issuance of securities, keeping of accounts, filing reports, etc. As to all these activities, however, there are sound reasons why regulation should be imposed, if at all, when the non-carrier first brings the carrier under its power.[21] For example, the

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[20] *New York Central Securities Corp.* v. *United States*, 287 U. S. 12, relied on by the ICC (Br. 36, 38–39) and by Alleghany (Br. 63–64) to support the contention that Alleghany "acquired control" of the Bridge Company through the merger, is not in point. There this Court upheld an ICC order under Section 5 (2) authorizing Central, which already had stock control of the Big Four, to acquire control of it by lease.

That case, however, involved an acquisition by a carrier, not (as here) by a non-carrier; in fact, the statute as it then stood did not provide for ICC approval of control acquisitions by non-carriers. As we have shown, Congress, in amending Section 5 in 1933 to subject non-carrier acquisitions of control to ICC regulation, did not cover all such acquisitions, but only those which result in the combination of previously separate carriers under common control.

In any event, a lease of railroad properties by a carrier to its immediate parent involves a far more significant change in the latter's control of the subsidiary than any change in a holding company's control of an indirect subsidiary which may result from the subsidiary's merger with another indirectly controlled carrier. See *supra*, pp. 27–28.

[21] As an alternative ground for its decision (see note 8, *supra*), the district court held that ICC approval was essential for Alleghany's acquisition of control of Central on the ground that Central constitutes "two or more carriers." At this point, we believe it unnecessary to discuss that issue.

possibility of financial impairment of a subsidiary carrier due to issuance of unsound securities by its parent arises when the latter first acquires control of the former.[22] Where, however, the holding company already controls the subsidiary, there is no occasion for inaugurating such regulation merely because of an intrasystem corporate reshuffling. Such a transaction, as the court below pointed out (R. 616), "is completely without significance so far as concerns the question whether the issuance of securities of the top corporation is subject to the jurisdiction of the I. C. C. * * *."[23]

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[22] This was recognized by Commissioner Eastman, who stated that the provision enacted as § 5 (3) "is necessary in the public interest, for in the event of a combination through such a holding company, the latter becomes a medium for financing and administering the affairs of the controlled railroad companies, and supervision of its operation will be just as essential as supervision of the operations of the carriers". Hearings before House Committee on Interstate and Foreign Commerce on H. R. 9059, 72d Cong., 1st Sess., p. 60.

[23] Both before the district court (R. 654) and before this Court, the ICC (Br. 26–36) and Alleghany (Br. 68–71) have relied on an alleged settled administrative interpretation of Section 5 (2) that intrasystem rearrangements constitute an acquisition of control by a non-carrier. The district court, after a careful review of the ICC decisions (R. 664–669), concluded that they were not consistent. That conclusion, we believe, was correct. Indeed, the ICC now argues (Br. 33) only that its decisions have been "almost" completely consistent since 1945, the year after the *Marshall Transport* case. But *Marshall Transport* held only that a non-carrier is a necessary party to an acquisition of control by its subsidiary; it did not decide whether an intrasystem rearrangement is such an acquisition. Thus, the critical date for considering the administrative interpretation on the latter issue is not 1945, but 1933, the year in which Section 5 was amended to give the ICC jurisdiction over acquisitions of control by non-carriers.

3. The practical effects of the limitation on ICC jurisdiction over non-carriers which we urge should also be noted. As far as the merger itself was concerned, the ICC had full power to determine whether it was "consistent with the public interest" without making the non-carrier a party. For Section 5 (2) (a) (i) also makes it unlawful "for two or more carriers to consolidate or merge their properties or franchises, or any part thereof," without ICC approval. Furthermore, since the Commission can approve the merger "subject to such terms and conditions and such modifications as it shall find to be just and reasonable" (Section 5 (2) (b)), it apparently could impose any conditions or changes necessary in the public interest to protect Central, a carrier which controls the merging carriers. Thus, denying the ICC the power to subject Alleghany to carrier status in connection with the merger would not impair the Commission's regulatory powers over the carriers themselves.

As far as the stockholders of the non-carrier are concerned, they would not lose any regulatory protection if the ICC does not have jurisdiction over their company. For if Alleghany is not "subject to regulation under the Interstate Commerce Act" (Section 3 (c) (9), Investment Company Act), then it is subject to regulation by the SEC, just as any other investment company. See *infra*, pp. 41–42. Indeed, since the primary public interest which the Investment Company Act was designed to protect is the "interest of investors," we suggest that regula-

tion of Alleghany under that Act would give investors at least as much, and perhaps more, protection than regulation under the Interstate Commerce Act.

B. THE 1945 STATUS ORDER, HAVING BEEN EXPRESSLY TERMINATED PRIOR TO THE STOCK ORDER, WAS INEFFECTIVE TO GIVE THE ICC JURISDICTION OVER ALLEGHANY

Alleghany (Br. 38–55) and the Gruss group (Br. 21–25) argue that, even if the ICC erred in subjecting Alleghany to carrier status in the merger proceedings, Alleghany nevertheless had such status by virtue of the 1945 status order.

The 1945 order provided that Alleghany was to be considered as a carrier "unless and until otherwise ordered by this Commission * * * (R. 185)." On March 2, 1955, however, Division 4 of the Commission did "order otherwise," for it expressly "terminated" that order and provided that it was of "no further force and effect." See *supra*, p. 7. On May 24, 1955, the full Commission affirmed. Thus, when the full Commission approved the preferred stock issuance on June 22, 1955, the 1945 order had been expressly terminated, in accordance with its terms, one month previously.[24]

The district court therefore correctly held that the 1945 order was ineffective to confer carrier status on Alleghany at the time of the stock order. Accordingly, it is unnecessary to consider the district court's alternative holding that the 1945 order terminated

[24] Division 4 approved the preferred stock issue on May 26, 1955, two days *after* the 1945 status order had been terminated.

automatically when Alleghany divested itself of control of C & O in 1954.[25]

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[25] The ICC and Alleghany further contend (ICC Br. 43–45; Alleghany Br. 84–86) that the Commission's order in the *Boston & Albany* proceedings (note 4, *supra*) also constitutes a jurisdictional basis for the preferred stock order. In that case, the ICC approved the acquisition by Alleghany and Central of three carriers which, although operated by Central under lease, were publicly owned. The argument is that, since Central thereby brought the acquired carriers for the first time under its direct control and thus under the indirect control of Alleghany, Alleghany therefore acquired control of the carriers under the *Marshall Transport* doctrine.

The principal difficulty with this argument (even assuming that Central's acquisition of the stock of the carriers whose properties were leased to it constituted "an acquisition of control" of the carriers by Alleghany) is that the Commission's order approving such acquisition did not provide that Alleghany was to be considered as a carrier. Section 5 (3) expressly states that a non-carrier shall "be considered as a carrier" only "*to the extent provided by the Commission in such order* * * *" [*i. e.*, one authorizing the non-carrier to acquire control of a carrier]. (Emphasis added.) Nor can the deficiency be cured by the fact, relied upon by appellants, that the Commission failed to include such a provision in the *Boston & Albany* order because it had already done so in the order (entered only 20 days earlier) relating to the merger of the Bridge Company. Under the Act, such a provision is an indispensable prerequisite to the ICC's jurisdiction over a non-carrier, and the ICC does not acquire jurisdiction because its order could have so provided.

III

THE INJUNCTION AGAINST CONSUMMATION OF THE PREFERRED STOCK EXCHANGE MAY PROPERLY BE VACATED BECAUSE OF THE CHANGE IN CIRCUMSTANCES

The district court not only set aside the ICC status and preferred stock orders, but further enjoined Alleghany from "taking any steps" in connection with or in furtherance of the issuance or transfer of the new preferred stock. The court reasoned that, since Alleghany was not subject to ICC jurisdiction at the time of the preferred stock issue, the latter was a transaction by an unregistered investment company in violation of Section 7 of the Investment Company Act; and that injunctive relief therefore was necessary to protect Alleghany's common stockholders from the irreparable injury they might suffer if denied the protection of the latter Act, namely, possible dilution of their equity through conversion of the new preferred stock.

The ICC (Br. 73–78) and Alleghany (Br. 95–98) argue that, even assuming that the district court correctly set aside the ICC orders, a three-judge district court convened to review ICC orders has no authority to enjoin threatened violations of the Investment Company Act. We believe, however, that the subsequent action of the SEC in denying Alleghany's preferred stock issue an exemption from the Investment Company Act obviates the further need for injunctive relief, and that this Court therefore properly may vacate the injunction without passing on the difficult question of its initial validity.

Section 7 of the Investment Company Act (15 U. S. C. 80a–1 *et seq.*) prohibits any unregistered investment company from offering for sale, selling, or delivering after sale, through the mails or in interstate commerce, any security. Since Alleghany was an unregistered investment company when the preferred exchange plan became effective upon approval by the ICC, and since the latter approval was invalid due to lack of ICC jurisdiction over Alleghany, the issuance of the 900,000 shares pursuant to the plan violated Section 7, as the district court held.[26] Furthermore, until Alleghany again registered with the SEC, it would also have been illegal for it to have issued or delivered the remaining 400,000 shares.

Alleghany's subsequent registration with the SEC neither validated the shares already issued nor permits issuance or delivery of the shares still on hand.[27] For Section 18 (d) of the Investment Company Act makes it unlawful for any registered management company (which Alleghany is) to issue any right to purchase which may be exercised during a period longer

[26] We agree with the district court that Alleghany's exemption from SEC regulation during the 1945–1955 period flowed from the Investment Company Act itself, and that the 1945 SEC order terminating Alleghany's registration under that Act "was but a formal recognition of that [statutory] exemption" (R. 657). Thus, when the ICC in May 1955 expressly terminated its 1945 status order (upon which its regulatory jurisdiction over Alleghany depended), Alleghany automatically again became subject to the Investment Company Act.

[27] Alleghany argues (Br. 99) that both the delivered and the undelivered portions of the preferred stock issue have already been validly issued under state law. But the status of such stock under state law does not determine its validity under overriding federal law.

than 120 days. In its decision of November 30, 1956, the SEC held that Alleghany's new convertible preferred stock was in fact such a right to purchase; that its issuance was unlawful unless exempted pursuant to Section 6 (c); and that the SEC could not retroactively grant such an exemption because it could not find that the exchange was "in the interest of investors."[28]

In the light of the SEC decision, we think it clear that subsequent consummation of the preferred stock exchange by Alleghany would constitute a "willful" violation of the Investment Company Act. Under Section 49 of that Act, such violations are subject to severe criminal penalties. Therefore, if this Court upholds the decision of the district court, presumably the threat of such penalties will be sufficient to deter Alleghany from attempting to consummate the exchange. We therefore suggest that the record before this Court discloses no present need for continuation of an injunction designed to protect the rights of Alleghany's common stockholders under the Investment Company Act.

Indeed, if the SEC should have reason to believe that Alleghany will disregard these criminal provisions, the SEC itself will have adequate opportunity itself to seek an appropriate injunction during the 25-day period which customarily intervenes between the judgment of this Court and issuance of the mandate. See Rule 59 (2), Revised Rules of this Court.

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[28] The SEC's opinion is set forth as an appendix to the SEC's *amicus* brief in this case.

For Sections 42 (e) and 44 of the Investment Company Act authorize the SEC to seek an injunction in the district court whenever it appears to it "that any person has engaged or is about to engage in any act or practice constituting a violation of any provision of this subchapter * * *," and directs the court to enter an appropriate "permanent or temporary injunction or decree or restraining order."

Because of the substantial change in circumstances, particularly the present availability of new and powerful sanctions against the same conduct forbidden by the injunction, the question of its initial validity, while not technically moot, is essentially of academic interest. The question, moreover, can certainly not be said to be a commonly recurring one; on the contrary, the case presents a largely unique factual situation. Accordingly, in this posture of the litigation, we believe there would be little purpose served by an exploration of the powers of three-judge district courts under the Urgent Deficiencies Act. Regardless of the initial validity of the injunction, the action of the SEC, the agency charged by Congress with the function of administering the Investment Company Act, has rendered continuance of the injunction unnecessary.

CONCLUSION

The judgment of the district court should be affirmed insofar as it sets aside the ICC status and preferred stock orders.[29] If the Court so affirms, we

[29] We note that, even if this Court were to agree with all of appellants' substantive arguments (*i. e.*, those other than review-

suggest that it may properly vacate the injunction against consummation of the preferred stock exchange.

Respectfully submitted.

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ability and standing), the case would apparently have to be remanded to the district court to consider issues raised below but not yet decided. Those issues are: (1) whether, as the plaintiffs' complaint alleged (R. 97–98), the preferred stock exchange plan was unfair to the common stockholders; and (2) whether, either as a matter of law or as an abuse of discretion, the ICC erred in denying the SEC's petition requesting the ICC to relinquish jurisdiction over Alleghany and thus to permit the SEC to regulate Alleghany as an investment company (R. 619–620).

APPENDIX

1. The pertinent provisions of the Interstate Commerce Act, 24 Stat. 379, as amended, 49 U. S. C. 5 (2), 5 (3), 5 (4), are as follows:

SEC. 5 (2) (a) It shall be lawful, with the approval and authorization of the Commission, as provided in subdivision (b)—

(i) for two or more carriers to consolidate or merge their properties or franchises, or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership; or for any carrier, or two or more carriers jointly, to purchase, lease or contract to operate the properties, or any part thereof, of another; or for any carrier, or two or more carriers jointly, to acquire control of another through ownership of its stock or otherwise; or for a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise; or for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise; or

(ii) for a carrier by railroad to acquire trackage rights over, or joint ownership in or joint use of, any railroad line or lines owned or operated by any other such carrier, and terminals incidental thereto.

(b) Whenever a transaction is proposed under subparagraph (a), the carrier or carriers or person seeking authority therefor shall present an application to the Commission, and thereupon the Commission shall notify the Governor of each State in which any part of

the properties of the carriers involved in the proposed transaction is situated, and also such carriers and the applicant or applicants (and, in case carriers by motor vehicle are involved, the persons specified in section 205 (e)), and shall afford reasonable opportunity for interested parties to be heard. If the Commission shall consider it necessary in order to determine whether the findings specified below may properly be made, it shall set said application for public hearing; and a public hearing shall be held in all cases where carriers by railroad are involved unless the Commission determines that a public hearing is not necessary in the public interest. If the Commission finds that, subject to such terms and conditions and such modifications as it shall find to be just and reasonable, the proposed transaction is within the scope of subparagraph (a) and will be consistent with the public interest, it shall enter an order approving and authorizing such transaction, upon the terms and conditions, and with the modifications, so found to be just and reasonable: *Provided,* That if a carrier by railroad subject to this part, or any person which is controlled by such a carrier, or affiliated therewith within the meaning of paragraph (6), is an applicant in the case of any such proposed transaction involving a motor carrier, the Commission shall not enter such an order unless it finds that the transaction proposed will be consistent with the public interest and will enable such carrier to use service by motor vehicle to public advantage in its operations and will not unduly restrain competition.

(c) In passing upon any proposed transaction under the provisions of this paragraph (2), the Commission shall give weight to the following considerations, among others: (1) The effect of the proposed transaction upon adequate transportation service to the public; (2) the effect upon the public interest of the inclusion,

or failure to include, other railroads in the territory involved in the proposed transaction; (3) the total fixed charges resulting from the proposed transaction; and (4) the interest of the carrier employees affected.

(d) The Commission shall have authority in the case of a proposed transaction under this paragraph (2) involving a railroad or railroads, as a prerequisite to its approval of the proposed transaction, to require, upon equitable terms, the inclusion of another railroad or other railroads in the territory involved, upon petition by such railroad or railroads requesting such inclusion, and upon a finding that such inclusion is consistent with the public interest.

(e) No transaction which contemplates a guaranty or assumption of payment of dividends or of fixed charges, shall be approved by the Commission under this paragraph (2) except upon a specific finding by the Commission that such guaranty or assumption is not inconsistent with the public interest. No transaction shall be approved under this paragraph (2) which will result in an increase of total fixed charges, except upon a specific finding by the Commission that such increase would not be contrary to public interest.

* * * * *

SEC. 5 (3) Whenever a person which is not a carrier is authorized, by an order entered under paragraph (2), to acquire control of any carrier or of two or more carriers, such person thereafter shall, to the extent provided by the Commission in such order, be considered as a carrier subject to such of the following provisions as are applicable to any carrier involved in such acquisition of control: Section 20 (1) to (10), inclusive, of this part, sections 204 (a) (1) and (2) and 220 of part II, and section 313 of part III, (which relate to reports, accounts, and so forth, of carriers), and section 20a (2) to (11), inclusive, of this

part, and section 214 of part II, (which relate to issues of securities and assumptions of liability of carriers), including in each case the penalties applicable in the case of violations of such provisions. In the application of such provisions of section 20a of this part and of section 214 of part II, in the case of any such person, the Commission shall authorize the issue or assumption applied for only if it finds that such issue or assumption is consistent with the proper performance of its service to the public by each carrier which is under the control of such person, that it will not impair the ability of any such carrier to perform such service, and that it is otherwise consistent with the public interest.

SEC. 5 (4) It shall be unlawful for any person, except as provided in paragraph (2), to enter into any transaction within the scope of subparagraph (a) thereof, or to accomplish or effectuate, or to participate in accomplishing or effectuating, the control or management in a common interest of any two or more carriers, however such result is attained, whether directly or indirectly, by use of common directors, officers, or stockholders, a holding or investment company or companies, a voting trust or trusts, or in any other manner whatsoever. It shall be unlawful to continue to maintain control or management accomplished or effectuated after the enactment of this amendatory paragraph and in violation of its provisions. As used in this paragraph and paragraph (5), the words "control or management" shall be construed to include the power to exercise control or management.

2. The pertinent provisions of the Investment Company Act of 1940, 54 Stat. 789, 15 U. S. C. 80a– *et seq.*, are as follows:

SEC. 3. * * *

* * * * * * *

(c) Notwithstanding subsections (a) and (b) of this section, none of the following persons is an investment company within the meaning of this subchapter and sections 72 (a) and 107 (f) of Title 11:

* * * * *

(9) Any company subject to regulation under the Interstate Commerve Act, or any company whose entire outstanding capital stock is owned or controlled by such a company * * * [15 U. S. C. 80a–3 (c) (9)].

* * * * *

SEC. 7. (a) No investment company organized or otherwise created under the laws of the United States or of a State and having a board of directors, unless registered under section 80a–8 of this title shall directly or indirectly—

(1) offer for sale, sell, or deliver after sale, by the use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security, whether the issuer of such security is such investment company or another person; or offer for sale, sell, or deliver after sale any such security or interest, having reason to believe that such security or interest will be made the subject of a public offering by use of the mails or any means or instrumentality of interstate commerce;

(2) purchase, redeem, retire, or otherwise acquire or attempt to acquire, by use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security, whether the issuer of such security is such investment company or another person;

(3) control any investment company which does any of the acts enumerated in paragraphs (1) and (2) of this subsection;

(4) engage in any business in interstate commerce; or

(5) control any company which is engaged in any business in interstate commerce.

The provisions of this subsection shall not apply to transactions of an investment company which are merely incidental to its dissolution. [15 U. S. C. 80a–7 (a)]

* * * * *

SEC. 18. * * *

* * * * *

(d) It shall be unlawful for any registered management company to issue any warrant or right to subscribe to or purchase a security of which such company is the issuer, except in the form of warrants or rights to subscribe expiring not later than one hundred and twenty days after their issuance and issued exclusively and ratably to a class or classes of such company's security holders; except that any warrant may be issued in exchange for outstanding warrants in connection with a plan of reorganization [15 U. S. C. 80a–18 (d)].

* * * * *

SEC. 42. * * *

* * * * *

(e) Whenever it shall appear to the Commission that any person has engaged or is about to engage in any act or practice constituting a violation of any provision of this subchapter and sections 72 (a) and 107 (f) of Title 11, or of any rule, regulation, or order thereunder, it may in its discretion bring an action in the proper district court of the United States, or the proper United States court of any Territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices and to enforce compliance with this subchapter and sections 72 (a) and 107 (f) of Title 11 or any rule, regulation, or order thereunder. Upon a showing that such person has engaged or is about to engage in any such act or practice, a permanent or temporary injunction or decree or restraining order shall be granted without

bond. In any proceeding under this subsection to enforce compliance with section 80a–7 of this title, the court as a court of equity may, to the extent it deems necessary or appropriate, take exclusive jurisdiction and possession of the investment company or companies involved and the books, records, and assets thereof, wherever located; and the court shall have jurisdiction to appoint a trustee, who with the approval of the court shall have power to dispose of any or all of such assets, subject to such terms and conditions as the court may prescribe. * * * [15 U. S. C. 80a–41 (e)].

* * * * *

SEC. 44. The district courts of the United States and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have jurisdiction of violations of this subchapter and sections 72 (a) and 107 (f) of Title 11, or the rules, regulations, or orders thereunder, and, concurrently with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by, or to enjoin any violation of, this subchapter and sections 72 (a) and 107 (f) of Title 11 or the rules, regulations, or orders thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. A criminal proceeding based upon a violation of section 80a–33 of this title, or upon a failure to file a report or other document required to be filed under this subchapter and sections 72 (a) and 107 (f) of Title 11, may be brought in the district wherein the defendant is an inhabitant or maintains his principal office or place of business. Any suit or action to enforce any liability or duty created by, or to enjoin any violation of, this subchapter and sections 72 (a) and 107 (f) of Title 11 or rules, regulations, or orders thereunder, may be

brought in any such district or in the district wherein the defendant is an inhabitant or transacts business, and process in such cases may be served in any district of which the defendant is an inhabitant or transacts business or wherever the defendant may be found. * * * [15 U. S. C. 80a–43].

* * * * * *

SEC. 49. Any person who willfully violates any provision of this subchapter and sections 72 (a) and 107 (f) of Title 11 or of any rule, regulation, or order thereunder, or any person who willfully in any registration statement, application, report, account, record, or other document filed or transmitted pursuant to this subchapter and sections 72 (a) and 107 (f) of Title 11 or the keeping of which is required pursuant to section 80a–30 (a) of this title makes any untrue statement of a material fact or omits to state any material fact necessary in order to prevent the statements made therein from being materially misleading in the light of the circumstances under which they were made, shall upon conviction be fined not more than $10,000 or imprisoned not more than two years, or both; but no person shall be convicted under this section for the violation of any rule, regulation, or order if he proves that he had no actual knowledge of such rule, regulation, or order [15 U. S. C. 80a–48].

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In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 36

ALLEGHANY CORPORATION, ET AL., APPELLANTS

v.

BRESWICK & CO., ET AL., AS COMMON STOCKHOLDERS OF ALLEGHANY CORPORATION, ETC.

No. 82

BAKER, WEEKS & CO., ET AL., APPELLANTS

v.

BRESWICK & CO., ET AL.

No. 114

INTERSTATE COMMERCE COMMISSION, APPELLANT

v.

BRESWICK & CO., ET AL.

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION, AMICUS CURIAE

OPINIONS BELOW

The opinion of the district court on final judgment (R. 651–673) is reported in 138 F. Supp. 123. Two

supplemental opinions (R. 674–675, 680) are not reported; memorandum opinions denying motions for new trial and for reargument (R. 675–680) are reported in 138 F. Supp. 138. The opinions on application for an interlocutory injunction (R. 601–639) are reported at 134 F. Supp. 132. The opinions denying a stay pending appeal (R. 639–642) are not reported; the opinion of Mr. Justice Harlan granting a partial stay (R. 643–650) is reported in 75 Sup. Ct. 912.

The reports of Division 4 (R. 414–446) and of the full Commission (R. 506–515) in the merger proceedings are reported in 290 I. C. C. 725 and 295 I. C. C. 11, respectively. The opinions of Division 4 in the preferred stock exchange (R. 518–537) and in the Boston and Albany acquisition proceedings (R. 450–471) are not reported.

JURISDICTION

The judgment of the district court was entered on December 23, 1955 (R. 555–557) and motions for a new trial and for reargument (R. 675–680) were denied on January 27, 1956. Notices of appeal were filed by appellants in No. 36 on January 31, 1956 (R. 3–22); February 1, 1956 (R. 22–24); and February 3, 1956 (R. 30–31); in No. 82 on February 23, 1956 (R. 24–30); and in No. 114 on March 26, 1956 (R. 1–2). Probable jurisdiction was noted in No. 36 on April 23, 1956 (R. 681), and in Nos. 82 and 114 on October 8, 1956 (R. 682).

STATUTES INVOLVED

Pertinent provisions of the Interstate Commerce Act and the Investment Company Act of 1940 are set forth in Appendix A, pp. 24–29, *infra*.

QUESTIONS PRESENTED

1. Where a company is excepted from the statutory definition of an "investment company" under the Investment Company Act of 1940, as "subject to regulation under the Interstate Commerce Act", whether it is necessary for such exception that the company be subject to the continuous supervisory jurisdiction of the Interstate Commerce Commission ("ICC").

2. Where an investment company's registration under the Investment Company Act of 1940 was terminated pursuant to an order of the Securities and Exchange Commission ("SEC") because the ICC had assumed regulatory jurisdiction over such company, whether the company becomes subject to the registration and other requirements of the Investment Company Act of 1940 after regulation by the ICC is no longer in effect, absent revocation by the SEC of its prior order.

3. Where securities are sold and delivered pursuant to a voluntary exchange offer in conformity with state law but in violation of the Investment Company Act of 1940, whether a court, otherwise having jurisdiction, may issue an injunction to prevent consummation of the exchange offer, if under that Act the issuance and delivery of such securities are declared void.

STATEMENT

Prior to June 1945 Alleghany Corporation ("Alleghany") was a registered investment company under the Investment Company Act of 1940, 54 Stat. 789, 15 U. S. C. 80a. In June of that year Alleghany owned approximately 600,000 shares of common stock of Chesapeake & Ohio Railroad Company ("C&O"), having a market value of approximately $31,500,000 which represented 38% of Alleghany's total assets of $83,000,000. About 86% of Alleghany's assets were then invested in securities of carriers, and only about 5% in securities of other companies (R. 194).

On the basis of Alleghany's control of the C&O and the C&O railroad subsidiaries, the Interstate Commerce Commission ("ICC") issued an order, dated June 5, 1945, pursuant to Section 5 (3) of the Interstate Commerce Act, declaring, among other things, that Alleghany be deemed a "carrier" subject to Sections 20 (1) to (10) inclusive and 20a (2) to (11) inclusive (R. 185).[1]

Thereafter Alleghany filed an application with the SEC to terminate its registration as an investment company pursuant to Section 8 (f) of the Investment Company Act. On October 4, 1945, the SEC, on the basis of the ICC's order and an examination of the provisions of the Interstate Commerce Act declared applicable to Alleghany, found that Alleghany was "subject to regulation under the Interstate Commerce Act", within the meaning of Section 3 (c) (9)

[1] Section 20 (1) to (10) of the Interstate Commerce Act relates to reports and accounts, and Section 20a (2) to (11) relates to issuance of securities and assumption of liabilities.

of the Investment Company Act and thus excepted from the statutory definition of an investment company. Accordingly, the SEC declared that Alleghany "has ceased to be and is not now an investment company", and ordered that Alleghany's registration "shall forthwith cease to be in effect, provided, however, that if in the future Alleghany Corporation ceases to be subject to regulation under the Interstate Commerce Act * * * this order may be revoked, suspended or modified after appropriate notice and opportunity for hearing" (R. 186).[18a]

Between 1945 and 1953 Alleghany's character as almost exclusively a railroad holding company changed drastically and assumed the business characteristics of an investment company with a varied portfolio of securities. By the end of 1953 Alleghany had disposed of all but 104,854 shares of the C&O stock and its investment portfolio consisted of securities of 28 different companies engaged in various businesses, including steel, oil, gas, aircraft, utility, transportation and manufacturing. The largest single investment consisted of a controlling block of the stocks of Investors Diversified Services, Inc. ("IDS"), a registered investment company under the Investment Company Act. IDS manages eight investment companies, which then had combined assets exceeding $1,000,000,000 and more than 500,000 security holders. Of Alleghany's total assets of approximately $56,800,000, on the basis of market values its transportation securities represented but 14% while its other investment securities represented 76%. Alle-

[18a] *Alleghany Corporation*, 20 S. E. C. 731, 735 (1945).

ghany's investments in transportation securities was further reduced to 8% of its total assets when it sold its remaining C&O stock on January 19, 1954. Also, between 1945 and 1953 Alleghany purchased 177 different securities issues with a total market value in excess of $128,000,000 and sold 151 of such issues with a total market value in excess of $130,000,000 (R. 195, 201; App. C, p. 71, *infra*).[2]

Alleghany, as noted, disposed of its remaining C&O stock on January 19, 1954. On June 22, 1954, the ICC directed Alleghany to show cause why its status as a carrier as determined by its 1945 order should not be revoked. On July 23, 1954, the ICC postponed its hearings, and subsequently, in September 1954, Alleghany joined in an application by the New York Central Railroad Company and its subsidiaries, pursuant to section 5 (2) of the Interstate Commerce Act, for approval of an intra-system merger and lease modification. In connection with this application, Alleghany sought a determination from the ICC that it be deemed a carrier by reason of its alleged control of New York Central, acquired subsequent to its disposition of the C&O stock (R. 423, 415).

In the meantime, in view of Alleghany's disposition of the C&O stock, the ICC's order to show cause, and the change in the character of Alleghany's investments since 1945, the SEC on July 7, 1954, issued a

[2] These purchases and sales did not include transactions in "joint ventures" in which Alleghany participated.

notice and order for hearing pursuant to the reservation of jurisdiction contained in its 1945 order (App. *C, infra*). Alleghany thereupon requested that the SEC postpone its hearing indefinitely until the ICC had determined whether Alleghany "shall continue to be 'subject to regulation under the Interstate Commerce Act'" in the pending ICC proceedings. Alleghany alleged before the SEC that it was then subject to such regulation by virtue of the 1945 order of the ICC, and stated that "should the ICC vacate its order, then the hearing in this proceeding would be unnecessary since Alleghany would revert to the jurisdiction of this Commission under the . . . [Investment Company] Act." (App. E, *infra*.) By stipulation the SEC proceedings were later postponed subject to call, Alleghany agreeing that (Appendix D, *infra*):

> if the Interstate Commerce Commission, before calling, revokes, modifies or suspends its order dated June 5, 1945 . . . in such manner as to relieve Alleghany from compliance with certain provisions of the Interstate Commerce Act specified in said order, then until the conclusion of the hearings herein Alleghany will not, without first obtaining the approval of this Commission, engage in any act or consummate any transactions which, if Alleghany were registered under the Investment Company Act of 1940, would by the terms of that Act either be prohibited or require an order of this Commission exempting or approving such transactions before their consummation.

The SEC also intervened in the pending ICC proceedings and filed a memorandum dated September 14, 1954, and a supplemental memorandum dated December 14, 1954. In these memoranda the SEC pointed out that in view of Alleghany's investment portfolio and investment activities, as noted above, Alleghany is an investment company within the definitions of that term as contained in Sections 3 (a) (1) and (3) of the Investment Company Act, and that the transactions in which Alleghany had been engaged were of a kind which Congress sought to be regulated for the benefit of public investors under the Investment Company Act. For these reasons, the SEC urged that Alleghany should no longer be deemed a "carrier" subject to regulation under the Interstate Commerce Act. Since under Section 5 (3) of the Interstate Commerce Act, Alleghany may be deemed a carrier "to the extent provided by the Commission in such order", the SEC suggested that the ICC, in its discretion, should limit its jurisdiction over Alleghany to any acquisition of carriers under Section 5 (2), and that, without "carrier" status, Alleghany would thus be subject to the broader and more comprehensive regulatory provisions of the Investment Company Act. It was pointed out that in fact the objectives of Section 5 (3) would be realized by the capital structure, accounting, reporting and other requirements of the Investment Company Act and that the administration of both agencies could be harmonized and given full effect (R. 191–210, 251–260).

The brief of the ICC (at pp. 7–17) fully describes its subsequent orders granting "carrier" status to Alleghany under Section 5 (3) of the Interstate Commerce Act and approving a voluntary exchange of an outstanding series for a new series of Alleghany preferred stock, and the review proceedings in the court below. It is sufficient to note here that the court below in its opinion of November 18, 1955, stated that it would, as it later did, vacate the status order and enjoin consummation of the exchange offer.

Thereafter, on December 9, 1955, Alleghany registered with the SEC as an investment company. By letter accompanying its registration Alleghany stated, *inter alia,* that such registration was made subject to its right to take the present appeal and its right to contend that because the 1945 order of the SEC remained unrevoked it remains exempt from the provisions of the Investment Company Act.

Early in 1956 applications were filed with the SEC by Alleghany and by holders of its preferred stock, common stock and warrants seeking a declaration by the SEC that no approval or other action was required under the Investment Company Act with respect to the transactions involved in the exchange offer, or in the alternative, for the issuance of an order pursuant to Section 6 (c) of the Investment Company Act exempting such transactions from Section 7 as of the time of their occurrence. Public hearings were held, at which Randolph Phillips, Breswick & Co. and Clarence W. Bailey, holders of Alleghany common stock, who opposed the granting of

the applications, were permitted to intervene. Proposed finding and briefs were filed by the parties and the staff of the SEC. On November 30, 1956, the SEC, one Commissioner dissenting, issued its Findings and Opinion and Order denying the applications.[3]

Under the exchange plan, each share of Alleghany 5½% preferred stock, $100 par value, was exchangeable at the option of the holder for 10 shares of a new 6% preferred stock, $10 par value. The 10 shares of new stock were not redeemable prior to May 1, 1970, and were convertible into 47 shares of Alleghany common stock, upon payment of $3.75 per share of that stock. The conversion ratio was set so that the number of common shares into which the 10 new shares were convertible would have a market value at May 25, 1955, of $237 after deducting the required cash payment. The $237 is equivalent to the redemption price of the old stock including dividend arrears of $132 per share.

The SEC held that an exemption was required, that under Section 6 (c) an exemption may be granted *nunc pro tunc* with respect to the exchange offer, and that in determining the availability of the requested exemption, the exchange offer should be tested under the provisions of the Investment Company Act applicable to registered investment companies. The SEC found that the new security was a right to purchase, specifically outlawed by Section 18 (d) of the

[3] The Findings and Opinion and Order are set forth in Appendix B, *infra*.

Investment Company Act,* rather than a "senior security" which would have been exempt from this prohibition pursuant to Section 18 (c) (2). It stated that whether a security is a right to purchase "is not controlled by the nominal designation given the security but is rather appropriately based on a realistic appraisal of the rights and values attaching to it at time of issuance." The SEC pointed out that the expert testimony indicated that the new stock without the conversion feature would sell at some, or perhaps a substantial, discount from its par value, and that with the conversion feature the new stock exchanged for the old preferred stock was designed to sell for about $20 in excess of the $237 redemption claim. It found that the preferred stock attributes of the new stock are "clearly subordinate and probably have an indiscernible influence on its market value" and that the controlling feature of the new security is its value as a right to purchase common stock upon making the necessary cash payment.

The SEC stated that the record showed "the undisputed highly speculative and volatile nature of the new preferred stock with the difficulties inherent in its evaluation because of its character as a right to purchase, which renders its inappropriate in the capital structure of an investment company such as Alleghany." It noted that in any attempted evaluation of the new security consideration would have to be given to the many variables which, in addition to changes

* Section 18 (d), *inter alia*, prohibits the issuance of a "right to subscribe to or purchase a security * * * expiring not later than one hundred and twenty days after their issuance."

in the market prices of the securities in Alleghany's portfolio, might affect the net asset value of Alleghany's common stock.

The SEC concluded that the requested exemption from the statute could not be granted in view of the difficulties of evaluating the new security that would be imposed on investors, both present as well as prospective, to whom the safeguards of the statute extend, and in view of the fact that it was not able to find on the basis of the record that the exchange offer fell within the range of fairness. The SEC observed that the "statutory prohibition against long-term warrants and rights to purchase gives Congressional recognition to the fact that such securities are a speculative medium that introduce complicating and undesirable features into a corporate structure and which may impose serious difficulties upon investors in determining the intrinsic value not only of the warrant or the right to purchase but of all the securities affected in the corporate structure."

On the question of fairness, the SEC stated that the very experts introduced in support of the plan differed sharply as to the ultimate value of the new security. It pointed out that one expert believed that ten shares of the new security exchangeable for each share of old stock would attain a value in excess of $400 after final consummation of the plan. In the SEC's opinion this would appear to produce a grossly unfair result. The SEC noted that the other expert witness who testified in support of the plan originally shared the first expert's view but when he appeared

at the hearing stated he had changed his opinion. This difference and change of opinion the SEC concluded "not only demonstrates the unclear and conflicting nature of the record with respect to whether the plan is within the range of fairness but it also shows the complex problems which would face an ordinary investor seeking to appraise Alleghany's securities."

Commissioner Patterson in his dissenting opinion concluded that, since the new preferred stock carried with it a priority over the common stock as to distribution of assets and payment of dividends, it was a senior security as defined by Section 18 (g) of the Act and therefore specifically exempted by Section 18 (e) (2) from the prohibitions of Section 18. He was of the opinion on the basis of the record that the exchange offer fell within the permissible range of fairness and therefore qualified for an exemption.

ARGUMENT

The SEC takes no position on whether the court below correctly construed the relevant provisions of the Interstate Commerce Act or orders of the ICC thereunder; nor on the extent of the jurisdiction of the court below. The SEC's views, herein set forth, are submitted to aid this Court in resolving issues raised under the Investment Company Act by Petitioner in No. 36 to the extent that a resolution of these issues may be relevant to the disposition of the appeals before this Court.

I

THE STATUTORY EXCEPTION UNDER SECTION 3 (C) (9) OF THE INVESTMENT COMPANY ACT APPLIES ONLY TO A COMPANY SUBJECT TO CONTINUING REGULATION BY THE ICC

Alleghany contends (Brief, pp. 55–56) that, even without "carrier" status under Section 5 (3) of the Interstate Commerce Act and continuing regulation by the ICC under Sections 20 and 20a,[5] Alleghany comes within the exception of Section 3 (c) (9) of the Investment Company Act. According to Alleghany, for purposes of Section 3 (c) (9) it is sufficient that Alleghany made an acquisition which was approved by the ICC under Section 5 (2) of the Interstate Commerce Act.

We do not agree with this interpretation of Section 3 (c) (9). The test under that section is whether a company "is subject to regulation under the Interstate Commerce Act". The term "regulation" in the context of the Investment Company Act necessarily denotes a continuous supervisory jurisdiction on the part of the ICC over certain of the internal affairs of the subject company. Hence the exception applies only when a company is subject to continuing ICC supervision. It was not the intention of the Congress to absolve a company, otherwise an investment company, from complying with the Investment Company Act because on occasion it makes an acquisition which requires approval by the ICC under Section 5 (2) of the Interstate Commerce Act, but which does

[5] See note 1, *infra*.

not impose upon it the type of continuous ICC regulation which may be required under Section 5 (3) of that Act.

The legislative history of Section 3 (c) (9) makes it clear that it was intended to avoid the "conflict and confusion" which might arise if companies were subjected to the jurisdiction of both the ICC and SEC in respect of the issuance of securities, the manner of keeping accounts and records, and the filing of reports.[6] As to a company such as Alleghany, these obligations under the Interstate Commerce Act arise only when specifically so ordered by the ICC under Section 5 (3).

The SEC has consistently interpreted Section 3 (c) (9) in the manner herein urged. In *The Atlantic Coast Line Company,* 9 S. E. C. 680 (1941), Section 3 (c) (9) was declared inapplicable to a railroad holding company which had not been ordered subject to ICC regulation under Sections 20 and 20a of the Interstate Commerce Act. Also, in *Alleghany Corporation,* 20 S. E. C. 731 (1945), it was only when the ICC in 1945 had declared Alleghany a "carrier" and imposed upon it the obligation to comply with specified provisions of Sections 20 and 20a, that Alleghany was deemed to come within the exception of Section 3 (c) (9).

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[6] See Senate Hearings on S. 3580, 76th Cong., 3rd Sess., Part 2, pp. 777–778.

II

REVOCATION BY THE SEC OF ITS OWN 1945 ORDER WAS NOT REQUIRED FOR ALLEGHANY TO BECOME SUBJECT TO THE INVESTMENT COMPANY ACT

The SEC order of 1945 terminating Alleghany's registration, issued pursuant to Section 8 (f) of the Investment Company Act, provided, *inter alia*, that it "may be revoked, suspended or modified" if "in the future Alleghany ceased to be subject to regulation under the Interstate Commerce Act" (R. 186). Alleghany argues (Brief, pp. 50–51) that until this order is revoked, it provides a continuing exemption and Alleghany may engage in any transaction without registering and otherwise complying with the Investment Company Act, even after the 1945 ICC order is revoked and even if the ICC orders under review are of no effect.

This argument is inconsistent with the regulatory scheme of the Investment Company Act, and misconceives the nature of the SEC order. In our view, when Alleghany ceased to be subject to regulation by the ICC, it became subject to the Investment Company Act without a formal order of revocation by the SEC of its own 1945 order.

Under the Investment Company Act the responsibility for registration rests upon the company, since that obligation is imposed upon every company, the character of whose business brings it within the definition of Section 3 (a). Section 3 (a) (1) defines an "investment company" as "any issuer which is or holds itself out as being engaged primarily, or pro-

poses to engage primarily, in the business of investing, reinvesting or trading in securities."[7] The Investment Company Act contains no provision for an administrative proceeding to declare a company to be an investment company and hence required to register thereunder. In this respect the Investment Company Act differs fundamentally from Section 5 (3) of the Interstate Commerce Act under which a holding company acquires carrier status only after the ICC has issued an order to that effect.[8] Unless registered, an investment company is prohibited under Section 7 from engaging in any transaction in interstate commerce or by the use of the mails, including the sale or disposition of securities, and under Section 47 (b) contracts relating to such transactions are void. In addition to criminal sanctions, the SEC, under Section 42 (e), may institute judicial proceedings and enforce compliance with Section 7, and the court may take exclusive jurisdiction of the company and appoint a trustee.

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[7] Cognate definitions are set forth also in paragraphs (2) and (3) of Section 3 (a), the latter being subject to certain exceptions and exemptions under Section 3 (b).

[8] The provisions of the Investment Company Act in this respect are not unique. Section 5 of the Public Utility Holding Company Act of 1935, 49 Stat. 803, 15 U. S. C. 79e provides for the registration of holding companies as therein defined, and Section 4 thereof prohibits a company which fails to register from engaging, directly or indirectly, in any transactions in interstate commerce. The SEC may enforce compliance with Section 4 of that statute. Failure to register may also give rise to a derivative suit for damages. See *Goldstein* v. *Groesbeck*, 142 F. 2d 422 (C. A. 2), *certiorari denied*, 323 U. S. 737.

When a company is registered under the Investment Company Act and thereafter ceases to be an investment company as defined therein, Section 8 (f) provides for cancellation of its registration. The effect is to relieve the company of those obligations which the Act imposes on registered companies. Until released by a Section 8 (f) order a company remains subject to the obligations of a registered investment company.* The 1945 SEC order under Section 8 (f) gave legal recognition to Alleghany's new status as a "carrier" subject to ICC regulation, as found by the SEC. That order, however, did not confer an exempt status upon Alleghany which continues beyond the existence of the facts upon which the Section 8 (f) order was based. Upon receiving its Section 8 (f) order, Alleghany assumed, in relation to the Investment Company Act, the position of any other company, such as banks, insurance companies, underwriters, charitable institutions, and other unregistered companies excluded under Section 3 (c)

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* In this connection the court below indicated that it disagreed with the statement *In re The United Corporation*, 128 F. Supp. 725 (D. Del.), that a company remains subject to the requirements of the Holding Company Act, even though it no longer has any public-utility subsidiaries, until its registration under the statute is terminated by a formal order of the SEC (R. 660). We believe, however, that the court in the *United* case was correct. On appeal in that case, *In re The United Corporation*, 232 F. 2d 601, 606 (C. A. 3), the court said: "United would cease to be subject to requirements for *registered holding companies* only by an order of the Commission issued upon such terms and conditions as the Commission finds and 'in such order prescribes as necessary for the protection of investors * * *' § 5 (d)." (Emphasis in original).

from the statutory definition of an investment company in Section 3 (a).

Upon a material change of facts removing the basis for Alleghany's continued claim to exception under Section 3 (c) (9), it would be incumbent upon Alleghany to register and otherwise to comply with the Investment Company Act. The company is not relieved from these statutory obligations merely because the Section 8 (f) order contained a reservation of jurisdiction for its revocation.[19] We believe this construction to be proper and necessary to achieve the objectives of the Act and to provide for orderly determination of jurisdiction. The responsibility must lie with the company to comply with the Act whenever later events remove the basis for exception. Alleghany in substance has recognized that absent ICC regulatory jurisdiction, it was subject to SEC jurisdiction (p. 7, *supra*).

Moreover, we do not agree, even on Alleghany's assumption that the 1945 SEC order conferred an exempt status which remains in effect until the order is revoked, that pending such revocation Alleghany may, without being subject to restraint, engage in any transaction which, but for the alleged exemption, would be prohibited or would require administrative approval. The decision in *SEC* v. *Long Island Lighting Co.*, 148 F. 2d 252 (C. A. 2), *certiorari granted*, 324 U. S. 837, and va-

[19] Section 8 (f) of the Investment Company Act does not provide in terms for an administrative proceeding to revoke an order thereunder if the conditions for the statutory exclusion no longer prevail. It is to be distinguished from Section 3 (b) (2) providing for a declaration of non-investment company status for particular companies, which provides for revocation only after notice and opportunity for hearing.

cated for mootness, 325 U. S. 833, upon which Alleghany relies (Brief, p. 43), was thereafter repudiated by the court in *West India Fruit & Steamship Co.* v. *Seatrain Lines, Inc.*, 170 F. 2d 775 (C. A. 2). In that case, referring to its prior decision in the *Long Island* case, the court said (170 F. 2d at 779) that "this court as at present constituted does not agree with that decision," and specifically held that a court has the power to grant an injunction to preserve the status quo until an agency determines whether it had statutory jurisdiction and the manner in which it should exercise it. *Cf. Hecht Co.* v. *Bowles*, 321 U. S. 321, 330. In the instant case, it is conceded that, without the availability of the exception under Section 3 (c) (9), Alleghany would be subject to SEC jurisdiction, and, as noted, the SEC has determined that the exchange offer did not meet the standards of Section 18 (d). Alleghany should not, therefore, obtain in this proceeding an affirmative ruling by this Court that, pending a formal revocation by the SEC of its 1945 order, Alleghany cannot be restrained from consummating the exchange offer.

III

THE SALE AND DELIVERY OF THE NEW STOCK, IF SUBJECT TO THE INVESTMENT COMPANY ACT, WAS IN VIOLATION OF THAT ACT

Alleghany contends (Brief, pp. 98–99) that since the new stock was validly issued under the law of Maryland, its state of incorporation, non-compliance with Federal law affords no basis for injunctive relief even, assuming that the district court, under the Urgent

Deficiencies Act, otherwise has the power to enjoin the exchange offer. But the law of Maryland does not govern the validity and transferability of the new stock issued or delivered in contravention of a paramount Federal statute.[11] If Alleghany was subject to the Investment Company Act, the issuance of 1,300,000 shares of new stock and the delivery of 900,000 shares were clearly in violation of Section 7 (a) (1), as would be the delivery of the 400,000 shares still held by the exchange agent. That section provides that an investment company, which is not registered, shall not directly or indirectly "offer for sale, sell, or deliver after sale, by the use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security * * *".[12] An injunction to restrain violation of these provisions is clearly proper.

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[11] *Otis & Co.* v. *SEC*, 323 U. S. 624; *First Iowa Hydro-Electric Cooperative* v. *F. P. C.*, 328 U. S. 152; *Illinois Natural Gas Company* v. *Central Illinois Public Service Company*, 314 U. S. 498.

[12] *Pacific National Bank* v. *Eaton*, 141 U. S. 227 and *Baltimore City Pass. Ry. Co.* v. *Hambleton*, 77 Md. 341, 26 A. 279 (1893) cited by Alleghany do not deal with situations involving a violation of law and are inapposite.

In the absence of ICC jurisdiction the exchange offer also was subject to the registration requirements of the Securities Act of 1933. Section 5 of that Act makes unlawful the sale or delivery after sale of any security not registered under the statute. The new stock was not registered because Alleghany claimed an exemption from the Securities Act pursuant to Section 3 (a) (6) thereof exempting securities "issued by a common or contract carrier, the issuance of which is subject to the provisions of Section 20a of the Interstate Commerce Act, as amended." If this court determines that Alleghany is not a "carrier" and the issuance of its stock therefore not subject to ICC approval under Section 20a, this exemption was not available.

Alleghany contends (Brief, p. 98) that securities sold in violation of Section 7 are not void because that section does not specifically so declare. This argument overlooks the provisions of Section 47 (b) of the Investment Company Act which provides that:

> every contract made in violation of any provision of this title * * * and every contract * * * the performance of which involves a violation of, or the continuance of any * * * practice in violation of, any provision of this title * * * shall be void (1) as regards the rights of any person who, in violation of any such provision * * * shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision * * *.

As previously stated, the sale and delivery of the new stock are in violation of Section 7 of the Investment Company Act and would not be in the public interest and interest of investors because, as the SEC found, the new stock contravenes the standards of Section 18 (d) of that Act.[13]

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[13] *A. C. Frost & Co.* v. *Coeur D'Alene Mines Corp.*, 312 U. S. 38, cited by Alleghany, arose under the Securities Act of 1933. It involved an option contract for treasury stock, the registration of which was required because the shares had been publicly offered by the optionee. This Court found the contract to be enforceable, even though the stock was unregistered, pointing out that no provision of that statute declared contracts relating to sales of unregistered shares to be void and that to consider such contracts void "would probably seriously hinder rather than aid the real

CONCLUSION

Accordingly, it is respectfully submitted that those contentions of Alleghany which are answered herein are without merit. As to other issues discussed by the parties, the Securities and Exchange Commission takes no position.

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Securities and Exchange Commission.

JANUARY 1957.

The Solicitor General, believing that the Court should be apprised of the position of the Securities and Exchange Commission in this case, authorizes the filing of this brief. In doing so, he intimates no opinion as to the merits of the views expressed by the Commission except insofar as they accord with those stated in the brief for the United States.

J. LEE RANKIN,
Solicitor General.

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purpose of the statute" of protecting innocent purchasers of securities (312 U. S. at 43).

It may be observed that as of the time that the restraining order was issued by the district court only 2400 shares had been sold on the New York Stock Exchange by the exchanging stockholders (R. 604), and, while not specifically disclosed by the record, that, after the stay granted by Mr. Justice Harlan, further sales have been extremely limited because of the trading restrictions imposed in the public securities markets (App. B, pp. 37–38, *infra*).

APPENDIX A

The pertinent provisions of the Investment Company Act of 1940, 54 Stat. 789, 15 U. S. C. 80a–*et seq.*, are as follows:

SEC. 3. (a) When used in this title, "investment company" means any issuer which—

(1) is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities;

(2) is engaged or proposes to engage in the business of issuing face-amount certificates of the installment type, or has been engaged in such business and has any such certificate outstanding; or

(3) is engaged or proposes to engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40 per centum of the value of such issuer's total assets (exclusive of Government securities and cash items) on an unconsolidated basis.

As used in this section, "investment securities" includes all securities except (A) Government securities, (B) securities issued by employees' securities companies, and (C) securities issued by majority-owned subsidiaries of the owner which are not investment companies.

(b) Notwithstanding paragraph (3) of subsection (a), none of the following persons is an investment company within the meaning of this title:

(1) Any issuer primarily engaged, directly or through a wholly-owned subsidiary or subsidiaries, in a business or businesses other than

that of investing, reinvesting, owning, holding, or trading in securities.

(2) Any issuer which the Commission, upon application by such issuer, finds and by order declares to be primarily engaged in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities either directly or (A) through majority-owned subsidiaries or (B) through controlled companies conducting similar types of businesses. The filing of an application under this paragraph by an issuer other than a registered investment company shall exempt the applicant for a period of sixty days from all provisions of this title applicable to investment companies as such. For cause shown, the Commission by order may extend such period of exemption for an additional period or periods. Whenever the Commission, upon its own motion or upon application, finds that the circumstances which gave rise to the issuance of an order granting an application under this paragraph no longer exist, the Commission shall by order revoke such order.

(3) Any issuer all the outstanding securities of which (other than short-term paper and directors' qualifying shares) are directly or indirectly owned by a company excepted from the definition of investment company by paragraph (1) or (2) of this subsection.

(c) Notwithstanding subsections (a) and (b), none of the following persons is an investment company within the meaning of this title:

* * * * *

(9) Any company subject to regulation under the Interstate Commerce Act, or any company whose entire outstanding capital stock is owned or controlled by such a company * * *

* * * * *

SEC. 6. * * *

* * * * *

(c) The Commission, by rules and regulations upon its own motion, or by order upon application, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation thereunder, if and to the extent that such exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of this title.

* * * * *

SEC. 7. (a) No investment company organized or otherwise created under the laws of the United States or of a State and having a board of directors, unless registered under section 8 of this title shall directly or indirectly—

(1) offer for sale, sell, or deliver after sale, by the use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security, whether the issuer of such security is such investment company or another person; or offer for sale, sell, or deliver after sale any such security or interest, having reason to believe that such security or interest will be made the subject of a public offering by use of the mails or any means or instrumentality of interstate commerce;

(2) purchase, redeem, retire, or otherwise acquire or attempt to acquire, by use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security, whether the issuer of such security is such investment company or another person;

(3) control any investment company which does any of the acts enumerated in paragraphs (1) and (2) of this subsection;

(4) engage in any business in interstate commerce; or

(5) control any company which is engaged in any business in interstate commerce.

The provisions of this subsection shall not apply to transactions of an investment company which are merely incidental to its dissolution.

* * * * *

SEC. 8. * * *

* * * * *

(f) Whenever the Commission, on its own motion or upon application, finds that a registered investment company has ceased to be an investment company, it shall so declare by order and upon the taking effect of such order the registration of such company shall cease to be in effect. If necessary for the protection of investors, an order under this subsection may be made upon appropriate conditions. The Commission's denial of any application under this subsection shall be by order.

* * * * *

SEC. 18. * * *

* * * * *

(d) It shall be unlawful for any registered management company to issue any warrant or right to subscribe to or purchase a security of which such company is the issuer, except in the form of warrants or rights to subscribe expiring not later than one hundred and twenty days after their issuance and issued exclusively and ratably to a class or classes of such company's security holders; except that any warrant may be issued in exchange for outstanding warrants in connection with a plan of reorganization.

(e) The provisions of this section 18 shall not apply to any senior securities issued or sold by any registered closed-end company—

* * * * *

(2) for the purpose of refunding through payment, purchase, redemption, retirement, or exchange, any senior security of such registered investment company except that no senior security representing indebtedness shall be so issued or sold for the purpose of refunding any senior security which is a stock; or

* * * * * *

(g) Unless otherwise provided: "Senior security" means any bond, debenture, note, or similar obligation or instrument constituting a security and evidencing indebtedness, and any stock of a class having priority over any other class as to distribution of assets or payment of dividends; and "senior security representing indebtedness" means any senior security other than stock.

* * * * * *

SEC. 42. * * *

* * * * * *

(e) Whenever it shall appear to the Commission that any person has engaged or is about to engage in any act or practice constituting a violation of any provision of this title or of any rule, regulation, or order thereunder, it may in its discretion bring an action in the proper district court of the United States, or the proper United States court of any Territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices and to enforce compliance with this title or any rule, regulation, or order hereunder. Upon a showing that such person has engaged or is about to engage in any such act or practice, a permanent or temporary injunction or decree or restraining order shall be granted without bond.

SEC. 47. * * *

* * * * * *

(b) Every contract made in violation of any provision of this title or of any rule, regulation, or order thereunder, and every contract hereto-

fore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this title, or any rule, regulation, or order thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, regulation, or order, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule, regulation, or order.

APPENDIX B

(Investment Company Act Release No. 2446)

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C.

November 30, 1956

IN THE MATTER OF ALLEGHANY CORPORATION

(Files Nos. 812-987, 812-988, 812-998)

(Investment Company Act of 1940—Section 6 (c))

FINDINGS AND OPINION OF THE COMMISSION

EXEMPTED TRANSACTIONS

Denial of Exemption
Exchange of Convertible Preferred Stock for Outstanding Preferred Stock with Arrearages
Issuance of Rights to Purchase

Convertible preferred stock, preferred stock attributes of which at time of issuance are clearly subordinate and probably have indiscernable influence on its market value, and predominant value of which attaches to its conversion right, *held,* not senior security entitled to exemption provided by Section 18 (e) of Investment Company Act but right to purchase within prohibition of Section 18 (d) of Act.

Where registered investment company makes application pursuant to Section 6 (c) of Investment Company Act for exemption from Section 7 with respect to partially consummated refunding plan,

adopted prior to its registration as an investment company, under which plan company's old preferred stock is exchangeable for new convertible preferred stock held by Commission to be right to purchase within prohibition of Section 18 (d) of Act, application *denied* under circumstances presented, particularly difficulties of investor evaluation introduced by new security and Commission's inability to find on basis of record that exchange falls within range of fairness.

* * * * *

We have before us applications seeking a declaration that no approval or other action on our part is now required under the Investment Company Act of 1940 ("the Act") with respect to transactions involved in a voluntary exchange of an outstanding series for a new series of preferred stock of Alleghany Corporation ("Alleghany"), a registered investment company, or in the alternative, the issuance of an order pursuant to Section 6 (c) of the Act exempting these transactions, as of the time of their occurrence, from the provisions of the Act.

The applications were filed by Alleghany and by holders of its preferred stock, common stock and warrants and the proceedings thereon were consolidated. After appropriate notice public hearings were held at which Randolph Phillips, Breswick & Co. and Clarence W. Bailey, holders of Alleghany common stock who oppose the granting of the applications, were permitted to intervene. Proposed findings and briefs were filed by the parties, after which our Division of Corporate Regulation ("the Division") submitted a recommendation that the requested exemption be granted but that because the issuance of the new preferred stock violated the Securities Act of

1933 the exemption be conditioned upon the making of an offer of rescission and registration under that statute. Exceptions were filed by Alleghany and the intervenors, and supplemental statements were filed by other stockholder participants. Oral argument was waived by the parties. On the basis of an independent examination of the record we make the following findings.

I. *Alleghany's Securities and the Exchange Offer*

At December 31, 1954, Alleghany had outstanding the following securities:

$7,496,000 principal amount 5% sinking fund debentures due 1962 and $14,000,000 notes payable to banks due in 1955 and 1956.

25,637 shares of $4 prior preferred convertible stock ("prior preferred stock"), entitled on redemption or liquidation, voluntary or involuntary, to $80 per share (an aggregate of $2,050,960) plus any accrued and unpaid dividends of which there are none, and convertible into 16 shares of common stock. Voting as a class the stock is entitled to elect two directors.

136,744 shares of 5½% Cumulative Preferred Stock, Series A, $100 par value, ("old preferred stock") entitled on redemption or voluntary liquidation to $105 per share (an aggregate of $14,358,120) or in involuntary liquidation to $100 per share (an aggregate of $13,674,400), plus in each instance accrued and unpaid dividends which amounted to $130.17 per share (an aggregate of $17,799,511). Because of the dividend arrearages the holders of this stock, voting as a class, were entitled to elect two directors.

4,641,125 shares of common stock, $1 par value, which, voting as a class, is entitled to elect four directors.

2,000,000 warrants for the purchase at any time of a like number of shares of common stock at a price of $3.75 per share ("perpetual warrants").

The present exchange plan was designed as a means of eliminating dividend arrears on the old preferred stock which have been accumulating since 1931, when dividend payments were discontinued, and which constitute a legal barrier to the payment of dividends on the common stock. From 1946, when it had 667,539 shares of old preferred stock outstanding, and continuing into 1953 Alleghany had been acquiring this stock through purchases and various exchange offers, all at a discount from the redemption value or liquidating claim of the stock. In 1954 when initial consideration was given to the present exchange plan Allegheny did not have cash in the amount needed to pay the arrearages in cash or to redeem the preferred stock, and because of bank loan restrictions Alleghany was not wholly free even to use available cash for payment of arrearages. The sale of a substantial portion of the company's assets to raise cash was not considered to be in the best interest of the common stockholders because it would result in contracting the company's business and reducing the common stockholders' equity. Nor was it deemed feasible to obtain the cash needed for retirement of the preferred claim by sale of new Alleghany securities on the open market.

The exchange offer was mailed to stockholders on February 10, 1955, following a special stockholders' meeting on February 8, 1955, at which the necessary charter amendments were approved, and the exchange has been partially consummated. Under the exchange offer each share of old preferred stock is exchangeable at the option of the holder, for ten shares of 6% Con-

vertible Preferred Stock, $10 par value ("new preferred stock"), a newly created issue junior to the prior preferred stock but senior to the old preferred stock and common stock. The new preferred stock is entitled to cumulative dividends at the rate of 6% per year, so that the annual dividend on the 10 shares of new preferred stock will be $6 as compared to the $5.50 per share annual dividend on the old preferred stock. The new preferred stock is entitled to payment in the event of involuntary liquidation of par value plus accrued dividends, and in the event of voluntary liquidation or redemption to 105% of par value plus accrued dividends, but it is not redeemable prior to May 1, 1970. It is convertible into shares of common stock upon payment of $3.75 per share of that stock. The number of shares of common stock into which each share of the new preferred stock is convertible was to be fixed on the last day on which the exchange offer could be accepted, so that as of that date the market price of such shares of common stock, less $3.75 per share representing the payment required on conversion, would be equal to approximately $237, equivalent to the redemption price of $105 per share of old preferred stock plus dividend arrearages of $132 per share on such stock. Voting as a class, the new preferred stock is entitled to elect two directors.

The exchange offer was subject to the entry on or before May 31, 1955, of an appropriate order by the Interstate Commerce Commission ("ICC") approving the securities to be issued, and to the acceptance of the offer by holders of 100,000 shares of the old preferred stock or such lesser number as Alleghany might elect to accept. The exchange offer was to be open until five days after the ICC issued its order of approval. As pointed out below, the ICC approved the proposal

subject to one change, which Alleghany adopted, and the necessary stockholders' acceptances were received.

II. *Injunction Proceedings*

Alleghany had in 1940 registered under the Act as a closed-end, non-diversified management investment company. On June 5, 1945, the ICC declared that Alleghany, by virtue of its stock ownership and control of the Chesapeake & Ohio Railway Company ("C & O"), was a carrier subject to certain provisions of the Interstate Commerce Act. In these circumstances Alleghany was excepted under Section 3 (c) (9) of the Investment Company Act from the definition of an investment company,[1] and on October 4, 1945, pursuant to Section 8 (f) of the Act, we ordered that Alleghany's registration as an investment company should cease to be in effect.[2]

Subsequently from time to time beginning in 1946 Alleghany disposed of part of its holdings of the C & O stock, culminating in the sale on January 19, 1954 of its residual block of such stock. Later in 1954 it acquired 586,800 shares of common stock of New York Central Railroad Company ("Central"). In September 1954 Alleghany joined in an application that had been filed by Central relating to an intrasystem merger, and in connection with that application Alleghany sought a determination from the

[1] Section 3 (c) (9) excepts from the definition of an investment company "Any company subject to regulation under the Interstate Commerce Act * * *."

[2] 20 S. E. C. 731 (1945). Section 8 (f) provides in pertinent part: "Whenever the Commission, on its own motion or upon application, finds that a registered investment company has ceased to be an investment company, it shall so declare by order and upon the taking effect of such order the registration of such company shall cease to be in effect."

ICC that it be deemed a carrier by reason of its alleged control of Central. In a separate application Alleghany sought approval of the exchange offer. This Commission in September and December 1954 filed with the ICC memoranda setting forth the view that Alleghany was primarily an investment company and that accordingly the ICC should in its discretion limit its jurisdiction to matters relating to any acquisition of a carrier by Alleghany, and that in other respects Alleghany should be subject to the broader and more comprehensive regulatory provisions of the Investment Company Act.

On March 2, 1955, the ICC, through its Division 4, terminated its 1945 order because of Alleghany's disposition of the C & O stock, but declared Alleghany a carrier subject to certain provisions of the Interstate Commerce Act, including those regarding the issuance of securities, because of Alleghany's acquisition of control over Central and its subsidiaries. This action was affirmed on May 24, 1955 by the ICC sitting en banc. On May 26, 1955, the ICC by order of its Division 4 authorized the issuance of the new securities contemplated by the offer, but required that the common stock market price establishing the conversion ratio be that of the last sale on May 25, 1955 rather than on the later date specified in the plan.[3] This condition was accepted by the Executive Committee of Alleghany's Board of Directors and the plan was appropriately modified. The closing price of Alleghany common stock on May 25, 1955, was 8¾.

[3] This action was taken to eliminate the possibility of manipulation of the common stock prices in order to influence the conversion rights of the new preferred stock, and also to make it possible for holders of the old preferred stock to determine prior to the last date of the exchange offer what the conversion ratio would be.

Under the conversion formula each share of new preferred stock became convertible into 4.7 shares of common stock, so that the 10 shares of new preferred stock to be received in exchange for one share of old preferred stock would be convertible into 47 shares of common stock on making the specified conversion payment. The exchange offer was accepted by holders of 132,344, or 96.8%, of the outstanding shares of old preferred stock.[4]

On June 23, 1955, following a denial by the ICC on the previous day of a petition for reconsideration filed by Breswick & Co. and Phillips, Alleghany instructed its transfer agent and its exchange agent to proceed with the distribution of the shares of new preferred stock under the exchange offer, and on that day 876,800 shares of new preferred stock were distributed and 446,640 shares were held for manual delivery against so called "window tickets". Late that day Alleghany was notified that a special three-judge court of the United States District Court for the Southern District of New York, in an action which had been brought early in June 1955 by Breswick & Co. and Phillips, had entered a temporary restraining order with respect to the exchange offer, which had the effect of preventing the further transfer of the shares of new preferred stock already delivered and the distribution of the undistributed shares.[5] The following day the New York Stock Exchange suspended trading in the new preferred stock and postponed settlement of such stock as had been traded either on a "regular way" or on a "when

[4] The holders of the old preferred stock were notified on May 27, 1955, that the plan had been changed pursuant to the ICC's order to fix the conversion ratio for the new preferred stock at 4.7 shares.

[5] *Breswick & Co.* v. *U. S.*, Civil Action No. 101–114.

issued" basis. Similar action was subsequently taken in the over-the-counter market.

The temporary restraining order was followed by a preliminary injunction entered by the District Court on July 26, 1955. On August 9, 1955, Mr. Justice Harlan of the United States Supreme Court stayed the preliminary injunction as to the new preferred stock which had been delivered, but transfer of these shares is severely limited because trading is still suspended. The preliminary injunction, as stayed by Mr. Justice Harlan, was made final on December 23, 1955. In its opinion[6] the District Court held that at the time Alleghany issued the new preferred stock it was not subject to regulation by the ICC under the Interstate Commerce Act but was subject to regulation by this Commission under the Investment Company Act and that under Section 7 of that Act the new preferred stock could not lawfully be issued because Alleghany was not then a registered investment company.[7] Appeals from this order have been taken to the Supreme Court of the United States.[8]

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[6] 138 F. Supp. 123.

[7] Section 7 (a) of the Act provides that no investment company unless registered shall directly or indirectly—

"(1) offer for sale, sell or deliver after sale, by the use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security * * *"

"(2) Purchase, redeem, retire or otherwise acquire or attempt to acquire, by use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security * * *"

[8] The intervenors, relying principally on the pendency of the appeals, have attacked our jurisdiction to consider the present applications, which they contend are in violation of the District Court injunction. This proceeding, however, does not conflict with, but rather complements, the jurisdiction of the courts. The

On December 9, 1955, Alleghany filed with this Commission a Notification of Registration as a closed-end, nondiversified management investment company pursuant to Section 8 (a) of the Act, and subsequently the applications now before us were filed.

III. *Applicable Statutory Standards*

As previously stated, the applications before us seek a declaration that no approval or other action on our part is now required under the Act with respect to the transactions involved in the preferred stock exchange. This request is predicated on the view that our order of October 4, 1945, which declared that Alleghany had ceased to be an investment company within the meaning of the Act, had the continuing effect of granting Alleghany an exemption from the Act when it issued the new preferred stock. That order terminated the registration of Alleghany but provided that "if in the future Alleghany Corporation ceases to be subject to regulation under the Interstate Commerce Act * * * this order may be revoked, suspended, or modified after appropriate notice and opportunity for hearing." The District Court rejected the view now urged upon us stating:

> "Alleghany contends, however, that the S. E. C. order * * * exempted Alleghany from the Investment Company Act; that, to bring Alleghany within the coverage of the Act required another S. E. C. order; and that no such order has been entered. We cannot agree for this reason: Section 3 (c) (9) of that Act, * * * exempts from that Act's provisions

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District Court held that Section 7 of the Act was applicable to Alleghany. This proceeding assumes that conclusion and is concerned with the application of that Section, a matter which is not before the courts and over which we have exclusive original jurisdiction.

> any company subject to I. C. C. regulation. The S. E. C. order * * * was but a formal recognition of that exemption, which became operative when the I. C. C. made its order of June 5, 1945, since, by that order, Alleghany became subject to I. C. C. regulation. When, however, at the latest on May 24, 1955, the June 5, 1945 I. C. C. order lost its efficacy, thereupon the S. E. C. order * * * became automatically inefficacious, with the result that Alleghany immediately became again subject to the Investment Company Act."[9]

Both Alleghany and the ICC have in their pending appeals to the United States Supreme Court from the order of the District Court raised the question of the jurisdiction of the District Court to enjoin a violation of Section 7. Unless and until the Supreme Court reverses the action of the District Court we shall abide by its holding, and shall view the transactions involved as subject to Section 7 of the Act. We accordingly decline to make the declaration requested by the applications.

The alternative request of the applications is that we enter an order pursuant to Section 6 (c) of the Act exempting the transactions involved in the exchange offer, as of the time of their occurrence, from the provisions of the Act. That section provides that we may exempt "any * * * transaction * * * from any provision" of the Act "if and to the extent that such exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and

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[9] *Brewick & Co.* v. *United States*, 138 F. Supp. 123, 129–130.

provisions of this title."[10] We have held that the broad power of exemption granted us under Section 6 (c) must not be so freely applied that the basic objectives of the Act are thwarted."[11] The propriety of granting relief largely depends upon the purposes of the particular section of the Act from which an exemption is necessary, the evils against which such section is directed, and the end which such section seeks to accomplish. In *American Participation, Inc.*[12] we observed with respect to our powers under Section 6 (c):

> The very breadth of a power to exempt any person, security, or transaction from any provision of the Act places upon us a grave responsibility that such power be exercised with the greatest circumspection. We must be alert to guard against the possibility that this Commission, established to implement the legislative will to protect investors, become the instrument through which the expressed policies of Congress are thwarted in case by case grants of exemption to any applicant who files and presses an application * * *

Insofar as the applications seek exemption from Section 7 of the Act, the object of which is to compel registration of investment companies by prohibiting an unregistered investment company from engaging

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[10] We have in appropriate cases granted exemptions under Section 6 (c) with respect to transactions that had already been consummated. *Hugh B. Baker*, 24 S. E. C. 202 (1946); *American Research & Development Corporation*, Investment Company Act Release No. 2254 (1955).

[11] *Petroleum and Trading Corporation*, 11 S. E. C. 389 (1942).

[12] 10 S. E. C. 431, 437 (1941). See also *Transit Investment Corporation*, 28 S. E. C. 10 (1948).

in transactions in interstate commerce or utilizing the mails, that objective of the Act is met since Alleghany is now registered. However, other standards of the Act are involved. In considering the present application, which seeks exemption of transactions previously undertaken when Alleghany was not registered as an investment company, the situation must also be viewed as though the exchange offer is now being proposed by Alleghany as a registrant and the provisions of the Act applicable under such circumstances apply. Such provisions include Sections 18 (d) and (e) which relate to types of securities which may be issued by registered investment companies, and any other provisions which bear upon the question under Section 6 (c) whether an exemption with respect to the exchange offer is "necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policies and provisions of the Act." Sections 25 (b) and 25 (c) relating to reorganizations of registered investment companies, although not directly authorizing us to approve or disapprove a plan of reorganization, reflect a Congressional concern with the fairness of plans of reorganizations for such companies,[12a] and we are of the view that it would be

[12a] Section 25 (b) of the Act authorizes us to render an advisory report as to the fairness of a plan of reorganization affecting a registered investment company for which solicitation of security holders is made, if such report is requested by the company or the holders of 25% of any class of its securities. Section 25 (c) of the Act authorizes a United States District Court in proceedings before it instituted by this Commission to enjoin the consummation of a plan for the reorganization of a registered investment company if the court determines that the plan is grossly unfair.

On January 14, 1955, Alleghany mailed to its stockholders a notice for special meeting on February 8, 1955, relating to the creation of the new preferred stock and authorization of addi-

inappropriate to make the finding that the exchange offer "is in the interest of investors," which is required in order to grant a Section 6 (c) exemption, unless we are satisfied that the offer falls within the range of fairness to the security holders affected.

Section 18 of the Act deals with standards for securities of registered investment companies, and subsection (d) prohibits such companies to issue "any warrant or right to subscribe to or purchase a security of which such company is the issuer, except in the form of warrants or rights to subscribe expiring not later than one hundred and twenty days after their issuance * * *."[13] Section 18 (e) (2) makes inapplicable the standards of Section 18 to a senior security issued by a closed-end company as part of a refunding, such as is here involved.[14] Section 18 (g) defines a senior security as "* * * any stock of a class having priority over any other class as to distribution of assets or payment of dividends * * *"

The intervenors contend that convertible securities contain in substance a warrant or right to purchase

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tional shares of common stock, and the notice was accompanied by a proxy statement explaining the exchange plan as then proposed. Since under Section 2 (a) (32) of the Act the exchange constituted a "reorganization", there was a "solicitation of security holders" within the meaning of Section 25 (b) and in addition the plan fell within the scope of Section 25 (c).

[13] The Alleghany perpetual warrants which are presently outstanding were issued pursuant to ICC authorization in 1952, when Alleghany was not subject to our jurisdiction under the Act.

[14] Section 18 (e) provides in pertinent part:

"The provisions of this section 18 shall not apply to any senior securities issued or sold by any registered closed-end company—

* * * * *

'(2) for the purpose of refunding through payment, purchase, redemption, retirement, or exchange, any senior security of such registered investment company * * *"

and are within the bar of Section 18 (d), in which case they can be issued only if we grant an exemption on the basis of appropriate findings that the standards set forth in Section 6 (c) are met. They also contend that an exemption cannot be granted because the exchange offer is unfair to the Alleghany common stockholders. On the other hand, Alleghany and the stockholders supporting the plan argue that the new preferred stock is not a warrant but is a senior security falling within the exemption of Section 18 (e) (2), and that the exchange offer is fair to all security holders. In deciding this issue we do not need to decide the impact of Section 18 (d) and 18 (e) upon any security other than the new preferred stock before us, which is not typical of convertible securities generally.

The statutory prohibition against long-term warrants and rights to purchase gives Congressional recognition to the fact that such securities are a speculative medium that introduce complicating and undesirable features into a corporate structure and which may impose serious difficulties upon investors in determining the intrinsic value not only of the warrant or the right to purchase but of all the securities affected in the corporate structure. A right to purchase common stock can thus confuse investors by the various implications and possibilities which it presents. A convertible security is by its very nature hybrid in character. In the instant case, this hybrid character derives, on the one hand, from the preferred aspects of the stock and, on the other, from the right to purchase common stock. It is unquestioned that if Alleghany sought to issue in exchange for the old preferred stock a non-convertible preferred stock plus a separate right to purchase, the latter would obviously not be a senior security but would be subject to the prohibition of Section 18 (d). The question,

therefore, is whether by changing the form and merging the two elements into a single security the statutory prohibition can be evaded.

In terms of its market value the new preferred stock is predominantly a right to purchase. Indeed, the exchange formula by which the conversion rights of the new preferred stock were determined was deliberately calculated to produce a market value far in excess of the par value of the preferred stock. The testimony of applicants own expert witnesses indicates that the new preferred stock without the conversion right would sell at some, or perhaps a substantial, discount from par, and that if similar rights were issued independently of any preferred stock they would have a value substantially the same as the new preferred stock.

The new preferred stock exchange for each share of old preferred stock was expected to sell for about $20 in excess of $237, the redemption value of the old preferred stock inclusive of the $132 of dividend arrears. Such price is $157 in excess of the par and involuntary liquidation value of the new preferred stock and $152 in excess of its voluntary liquidation preference. Such excess is made possible only because of the valuable right to convert into common stock embodied in the new preferred stock.

We recognize that if the value of the conversion right dropped because of a decline in the value of Alleghany's common stock, the value of the preferred stock attributes might become dominant, and that in a declining market or in liquidation the holders of the new preferred stock could be substantially better off than would be the holders of mere warrants. However, the preferred stock attributes of the new preferred stock are now clearly subordinate and probably have an indiscernible influence on its market

value. From the viewpoint of the fairness of the plan, that is, whether the preferred stockholders are being fairly compensated for the rights they are being asked to surrender, which is discussed below, the controlling feature is the value of the right to purchase common stock and not the preferred stock attributes.

In our view, the determination of whether a security is a senior security or a right to purchase within the meaning of the Act is not controlled by the nominal designation given the security but is rather appropriately based on a realistic appraisal of the rights and values attaching to it at the time of its issuance.[15] We think that in the present case the right to purchase common stock, which was purposely made the valuable element in the new preferred stock in order to induce exchanges, so dominates the investment characteristics of the new preferred stock as to make that stock in substance not a senior security entitled to the exemption provided by Section 18 (e) of the Act but a right to purchase within the meaning of the prohibition of Section 18 (d). The real consideration for exchanging the old preferred stock is not the priorities of the new security but its right to purchase common stock, and consequently the new security must be viewed as a right to purchase in applying the standards of the statute. We are of the opinion that under the circumstances presented, particularly the difficulties that would be imposed on investors, both present as well as prospective to whom the safeguards of

[15] Both the preferred stockholder applicants and Alleghany recognize that if for purposes of evading the Act a security were created which had the form of a senior security because it had a nominal senior claim but the substance of a warrant because all or virtually all of the value of the security was based upon the right to acquire a junior security, the security might properly be found to be a warrant within the meaning of Section 18 (d).

the statute extend, in evaluating this security were its issuance permitted, and the fact that we are not able to find on the basis of the record before us that the exchange offer falls within the range of fairness, we cannot grant an exemption under the standards of Section 6 (c). The speculative nature of the new preferred stock, the difficulty of its evaluation, and our consequent inability to make the necessary findings are demonstrated by the record, particularly the testimony of the two expert witnesses who testified in support of the plan. Before considering that testimony we examine the assets and income of Alleghany as they bear upon the exchange offer.

Alleghany's total net assets and net assets per share of old preferred stock and common stock in the years 1946–1954 are shown in the following table:

Year-end	Total Net Assets*	Net Assets Per Share*	
		Old Preferred	Common
1946	$55,719,552	$76.74	Deficit
1947	50,753,586	80.92	"
1948	42,412,552	86.24	"
1949	32,929,876	97.69	"
1950	37,941,785	142.25	"
1951	37,655,260	147.37	"
1952	41,511,995	265.42	1.50
1953	34,685,540	238.14	.40
1954	67,020,845	474.93	7.21

*For the years 1946–1953, inclusive, the figures presented are based on indicated market quotations of assets, except for certain unlisted securities and joint venture investments carried at cost. For 1954, the figures presented are based on market quotations for all investments.

The steady increase, except for 1953, shown in the above table in the asset coverage for the old preferred stock is attributable in part to increases in value of Alleghany's assets and in part to the retirement through repurchase or exchange of a large number of shares of old preferred stock and prior preferred stock at substantial discounts from their liq-

uidation values. Substantial changes have taken place in the composition of Alleghany's assets since 1946, when virtually all of its investments, exclusive of U. S. Government obligations, were in securities of carriers and its holdings of C & O common stock were its most substantial investment.

As shown on the following table, at December 31, 1955, Alleghany's assets aggregated $102,421,760, with its principal investments being in the common stock of Investors Diversified Services, Inc. ("IDS"), a registered investment company controlling or managing an important group of investment companies, and in direct holdings of Central common stock as well as in a half interest in a joint venture holding such stock:

Cash and Treasury Bills	$5,511,140
Notes Receivable	16,114,421
Guaranteed Joint Ventures [a]	14,207,385
681,400 shares of Central common stock [b]	31,599,925
Missouri Pacific Railroad Company common stock	8,514,000
IDS common stock	25,534,867
Miscellaneous other assets	940,022
Total	$102,421,760

[a] The joint venture held 330,000 shares of Central common stock and had approximately $2,200,000 invested in stock of Delhi-Taylor Oil Corporation and Lionel Corporation.

[b] In 1956 Alleghany acquired an additional 118,900 shares of Central common stock.

At the same date Alleghany's outstanding liabilities and securities senior to the preferred stock involved in the exchange offer aggregated approximately $23,000,000.

The following table shows Alleghany's annual gross and net income, exclusive of security transactions, its profits or losses from security transactions, and the

net income per share, exclusive of security transactions for the period 1946 to 1954.

Year	Gross Income from Dividends and Interest	Net Income (Loss) Exclusive of Security Transactions	Profit (Loss) from Sales of Investments	Net Income per Share of Stock (Exclusive of Profits or Losses from Security Transactions)	
				Old Preferred	Common
1946	$2,570,929	$1,593,776	$2,007,797	$2.16	(80.45)
1947	2,628,686	1,746,132	(13,747,895)	2.83	(.32)
1948	5,439,055	4,036,609	(6,235,210)	8.95	.33
1949	2,887,856	1,869,558	(5,583,016)	5.85	.02
1950	2,189,613	1,244,408	2,175,997	4.72	(.04)
1951	2,117,017	920,378	(605,037)	3.54	(.10)
1952	2,384,525	861,652	50,806	5.38	(.09)
1953	2,020,715	244,222	6,452,830	1.03	(.08)
1954	1,676,115	(105,247)	4,278,748	(0.15)	(.21)

In the period covered by the table, Alleghany had sufficient income only in 1948 and 1949 to cover the $5.50 per share current dividend preference of the old preferred stock, although as previously pointed out no dividends have been paid on that stock since 1931.[16]

A statement of income for Alleghany for the years 1954 and 1955 is attached as Appendix A. It shows total income from dividends and interest of $1,676,115 in 1954 and $2,511,379 in 1955, which after payment of substantial amounts of expenses, including over $800,000 of interest on debentures and bank loans, resulted in a net loss of $105,247 in 1954 and net income of $316,721 in 1955, exclusive of profits from security transactions of $4,278,748 in 1954 and $1,989,172 in 1955.

[16] Until 1950, Alleghany was barred by virtue of an existing capital deficit from paying any dividends. Beginning in that year, it paid dividend arrearages on a formerly outstanding prior preferred stock, and those arrears were eliminated in 1953 when most of the balance of the issue was exchanged for the presently outstanding prior preferred stock.

Alleghany's investments in the common stocks of Missouri Pacific Railroad Company and IDS yield no dividends. As of the end of 1955, Alleghany anticipated income in the immediate future only on the notes receivable it held and from its investments in Central common stock, on which dividends of 50¢ per share were paid in 1954 and which was placed on a $2 annual dividend basis in 1955.

The annual dividend requirement on Alleghany's outstanding prior preferred stock is $101,048 and on the 1,323,440 shares of new preferred stock issuable under the exchange offer $794,064, or an aggregate of $895,112. The record indicates that in formulating the exchange offer Alleghany, relying on the prospect that the Central common stock would be placed on a $2 annual dividend basis, anticipated that its income would be sufficient to meet the dividend requirements on the new preferred stock. It appears that payment of dividends on this stock, as well as on the common stock, was dependent upon the ability of Central to continue its present $2 dividend rate and some improvement in net portfolio income or upon the availability of profits from security transactions.

In any attempted evaluation of the new preferred stock, consideration would have to be given to the many variables which, in addition to changes in the market prices of the securities in Alleghany's portfolio, might affect the net assets value of the Alleghany common stock. On May 25, 1955, the date as of which the conversion ratio under the exchange offer was fixed, the Alleghany common stock had a net asset value of $8.79 per share. If effect were given to the issuance of the new preferred stock, such value would increase to $12.55. If the conversion of all the new preferred stock into common stock, the early occurrence of which the record indicates is not

likely, were assumed as of that date, the net asset value would have been $8.73 per share. These calculations, however, do not make allowance for the changes in asset value which would result from (1) the conversion into common stock of the 25,262 outstanding shares of prior preferred stock, each share of which has an $80 stated value and is convertible into 16 shares of common stock, or at an effective price of $5 per share; (2) the exercise of an option held by Robert R. Young, chairman of Alleghany's board of directors, to purchase 100,000 shares of common stock at $3.0625 per share until May 1, 1961; and (3) the exercise of the outstanding perpetual warrants to purchase approximately 2,000,000 shares of common stock at $3.75 per share. If conversion of these three items were assumed as of May 25, 1955, the asset value would have been reduced to $7.09 per share, and if it were further assumed that all of the shares of new preferred stock issued under the exchange offer were converted into common stock, the asset value of the common stock would have been $7.83.

Furthermore, while the record indicates that the likelihood of conversion of the preptual warrants is remote, it suggests that a somewhat greater likelihood exists for near-term conversion of the prior preferred stock, which sells at little or no premium and in which arbitrage activity may therefore cause conversions. If the common stock were placed on a favorable dividend basis, conversion of the prior preferred stock would be increased. It also appears highly likely that the option held by Young would be exercised before it expires in 1961. If conversion of the prior preferred and the exercise of Young's option were assumed as of May 25, 1955, the asset value of the common stock would have been $8.38 before giving

effect to the issuance of the new preferred stock, $11.77 after giving effect to the issuance of that stock, and $8.55 upon the further assumption that all the new preferred stock was converted into common stock.

On the basis of the various conversion hypotheses set forth above, but excluding any assumed exercise of the perpetual warrants, the 47 shares of common stock obtainable on conversion of the new preferred stock received under the exchange offer would have a net asset value ranging from approximately $217 to $413, depending on the extent of conversions assumed.

One of the expert witnesses who testified in support of the exchange offer was Winthrop Lenz, a partner in the securities firm of Merrill, Lynch, Pierce Fenner & Beane ("Merrill Lynch") which was furnished the plan as originally drafted by Alleghany so that that firm could determine whether it would underwrite the plan or agree to act as dealer-manager in effecting the exchange. After the plan was considered by Lenz and certain of his associates, Merrill Lynch advised Alleghany that it was prepared to act as dealer-manager provided the plan were modified, as it subsequently was, to include the 15-year non-callable feature of the new preferred stock and to increase the number of shares of common stock into which the new preferred stock would be convertible by providing that such number be computed on the basis of the closing market price of the common stock rather than, as the plan had originally provided, at such market price plus $1.[17]

[17] Lenz testified that in considering the plan Merrill Lynch wished to be sure that its customers, for whom it was record holder of over 25,000 shares of common stock and over 200,000 perpetual warrants, were not adversely affected by the offer and that it was also fair to the preferred stockholders.

Lenz testified that the exchange plan would have to offer enough to the holders of the old preferred stock to persuade them to surrender their claim for dividend arrears "for a conversion privilege which is a very intangible thing and which can shrink and expand very rapidly" as the price of the common stock changes. Lenz observed that preferred stockholders were being asked to give up a claim on redemption of $237 in exchange for new preferred stock having a par value of $100 with all the remaining value attaching to a highly volatile conversion privilege. Since under the plan a one-point decline in the common stock would be reflected in a 47 point decline in the preferred stock, Lenz stated that he and his associates felt that to induce the preferred stockholders to give up a considerable amount of security and assume the inherent risks involved in the conversion privilege it was necessary to offer a reasonable amount in excess of the total claim of $237 or somewhere between $250 and $260, which he characterized as a "maximum kind of premium."

Lenz and his associates were of the view that under the exchange plan as it was amended the 10 shares of new preferred stock issuable for a share of old preferred stock would have a market value of $250 to $260 as of the date the conversion ratio was fixed. They believed the conversion privilege alone would result in a market value of approximately $237, and that the non-callable provision would add to the market value of the new preferred stock about 50 cents per share of common stock obtainable upon conversion or an aggregate of no more than $20 or $30 on the basis of the then prevailing market prices for the

common stock.[18] Lenz pointed out that there is no scientific way of computing or estimating the premium value of a long-term option, and that such an estimate was a matter of judgment on the basis of past experience with other securities. He stated: "The difficult part, as I see it, is trying to determine just how much of this premium you would generate as a result of this plan and how it could be held within reasonable bounds. That unfortunately goes back to that matter of judgment that we have such difficulty with."

On the basis of the conversion ratio of 47 shares, the non-callable feature at fifty cents per share would add $23.50 in value to the new preferred stock, giving it a total market value as of May 25, 1955, of about $260. If the premium were as high as 75 cents—and it appears to have ranged from 26¢ to $1.56 and averaged 80¢ in the trading period between Alleghany's announcement of the conversion ratio and the suspension of trading—the total premium on the 47 shares applicable to one share of old preferred stock would be about $35, so that the total value for the old preferred stock as of May 25, 1955, when the conversion ratio was fixed, would be $270.[19] Lenz considered that such value would still fall within the range

[18] Lenz and his associates compared the new preferred stock with Alleghany's outstanding perpetual warrants, which at the time had a market value that reflected a premium attaching to the perpetual feature of the warrant of about $1.25, and took into account among other things that the preferred stock conversion right was a 15-year non-callable right as compared with a perpetual right for the warrant.

[19] The expert who testified in addition to Lenz stated that while the 15-year non-callable feature of the new preferred stock would have a value of between 50 cents and something less than $1 per share of common stock, its value was a matter of "guesswork" until the preferred stock was issued and a "normal" market obtained.

of fairness to the common stock, although it would be on the "high side" of the range.

In the period after the conversion ratio was fixed the price of the old preferred stock or its equivalent in new preferred stock rose substantially above $260 and sold as high as $352.50, and the price of the common stock reached as high as $10.75.[20] Inter-

[20] The following table covers the 20 trading days from May 27, 1955, when Alleghany announced the actual conversion ratio, until June 24, 1955, when trading was suspended and compares the closing price of the old preferred stock through June 6, 1955, and 10 shares of the new preferred stock as quoted on a when-issued basis beginning June 7, 1955, with the price of 47 shares of common stock obtainable on conversion of the ten shares of new preferred stock for which each share of old preferred stock is exchangeable under the exchange offer, and it also shows the resultant premium value apparently attributable to the 15-year non-callable feature of the new preferred stocks:

Closing Price As of	Common Stock	Old Preferred Stock*	Conversion Value of 47 Shares of Common Stock	Premium Value of 15-Year Non-Callable Right of New Preferred Stock	
				For 47 shs.**	For 1 Sh.
May 27	8⅛	277½	240⅞	36⅝	0.78
31	9½	292	270¾	21¼	.46
June 1	9⅜	300	287⅞	12⅛	.26
2	10	316	293¾	22¼	.47
3	9⅞	315	287⅞	27⅛	.58
6	9⅞	311	287⅞	23⅛	.49
7	9⅞	326¼	287⅞	38⅜	.82
8	10	340	293¾	46¼	.98
9	10	316¼	293¾	22½	.48
10	10⅛	323¾	299⅛	24⅝	.51
13	10⅛	333¾	299⅛	34⅝	.73
14	10	333¾	293¾	40	.85
15	10	348¾	293¾	55	1.17
16	10	346¾	293¾	52½	1.12
17	9⅞	340	287⅞	52⅛	1.11
20	9⅞	341¾	287⅞	53⅞	1.14
21	9⅜	337½	264⅝	73⅛	1.56
22	9¾	338¾	276⅛	62⅝	1.33
23	10⅜	348¾	329	19¾	.42
24	10½	352½	317¼	35¼	.75

* Prices are for old preferred stock through June 6, 1955, and for 10 shares of new preferred stock as quoted on a when-issued basis beginning June 7, 1955.

** After allowance for price of $3.75 per share payable on conversion.

Closing Price As of	Common Stock	Old Preferred Stock*	Conversion Value of 47 Shares of Common Stock	Premium Value of 15-Year Non-Callable Right of New Preferred Stock	
				For 47 shs.**	For 1 Sh.
May 27	8 7/8	277 1/2	240 7/8	36 5/8	0.78
31	9 1/2	292	270 1/4	21 3/4	.46
June 1	9 7/8	300	287 7/8	12 1/8	.26
2	10	316	293 3/4	22 1/4	.47
3	9 7/8	315	287 7/8	27 1/8	.58
6	9 7/8	311	287 7/8	23 1/8	.49
7	9 7/8	326 1/4	287 7/8	38 3/8	.82
8	10	340	293 3/4	46 1/4	.98
9	10	316 1/4	293 3/4	22 1/2	.48
10	10 1/8	323 3/4	299 5/8	24 1/8	.51
13	10 1/8	333 3/4	299 5/8	34 1/8	.73
14	10	333 3/4	293 3/4	40	.85
15	10	348 3/4	293 3/4	55	1.17
16	10	346 1/4	293 3/4	52 1/2	1.12
17	9 7/8	340	287 7/8	52 1/8	1.11
20	9 7/8	341 1/4	287 7/8	53 3/8	1.14
21	9 3/8	337 1/2	264 3/8	73 1/8	1.56
22	9 5/8	338 3/4	276 1/8	62 5/8	1.33
23	10 3/4	348 3/4	329	19 3/4	.42
24	10 1/2	352 1/2	317 1/4	35 1/4	.75

* Prices are for old preferred stock through June 6, 1955, and for 10 shares of new preferred stock as quoted on a when-issued basis beginning June 7, 1955.

** After allowance for price of $3.75 per share payable on conversion

vendors point to this price history as demonstrating the unfairness of the exchange offer. If the rise in the market price of the old preferred stock after the conversion ratio was fixed was due to a rise in the market price of the common stock attributable to the exchange offer rather than to independent factors such as an increase in the value of Alleghany's portfolio, it would be evidence of the offer's unfairness.

While Lenz considered that the rise in the market price of the Alleghany common stock reflected increases in its underlying asset value,[21] he thought that not all of the benefits realizable by the common stock from the plan were reflected in its market price in advance of the plan's consummation.[22] Lenz also pointed out that since a petition for reconsideration was pending before the ICC, the market price of the common stock during the period after the ICC's initial approval of the plan on May 26, 1955 and before the temporary restraining order issued on June 23, 1955 probably did not give full effect to the increase in asset value which would inure to the common stock

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[21] Thus, in the 20 trading days from May 25, 1955, Alleghany's common stock increased from 8¾ to as much as 10¾, and the underlying asset value increased by $2.13 per share of common stock, primarily as a result of rises in the prices of Central common stock from 40½ to 44¾ and of IDS stock from 65 to 82.

[22] Lenz did not express any opinion regarding the effect of changing the date as of which the conversion ratio was to be fixed from a date 5 days after an order of approval by the ICC, as originally proposed, to a date preceding the announcement of the ICC's approval. Since trading had proceeded on the assumption that the conversion ratio would be fixed after the ICC had approved the plan, it is likely that the market value of the common stock on May 25, 1955, did not fully reflect the benefits anticipated from the plan, particularly the increase in asset value because of the elimination of arrears on the old preferred stock. In any event, the full extent of this benefit would not be definitely known until the extent of acceptances was announced.

as a result of the plan. In Lenz' opinion, this increase and a corresponding increase in the price of the new preferred stock would occur after final consummation of the plan. As previously pointed out, on May 25, 1955, the date as of which the conversion ratio under the exchange offer was fixed, the Alleghany common stock had a net asset value of $8.79 per share, and if effect were given to the issuance of the new preferred stock, such value would increase to $12.55 by virtue of the elimination of the prior claim representing the dividend arrearages on the old preferred stocks. Lenz expressed the view that Alleghany's common stock would continue to sell at a premium over its asset value, as it had at times in the past, so long as that asset value was increasing, and that Alleghany's common stock might be expected to increase to approximately the $12.55 figure after final consummation.[23] On that basis the common stock into which each share of old preferred stock would be ultimately convertible would be in excess of $400, an amount which is considerably above the $270 figure that Lenz recognized as being high in terms of fairness to the existing common stockholders. In our opinion this would appear to produce a grossly unfair result.

Arthur M. Leinbach, a railroad security analyst for Kidder, Peabody & Co., the securities firm which submitted the successful offer to act as dealer manager for the exchange plan, also testified as an expert wit-

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[23] Lenz did not believe that the possibility of ultimate conversion of the new preferred stock, and the consequent diluting effect on asset value, would hold down the market price of the common stock, since such conversions were not a likely prospect for 15 years. In our opinion, this illustrates the potentially deceptive effect on investors of the right to purchase common stock which the new preferred stock represents.

ness and expressed the opinion that the exchange offer was fair both to the preferred and common stockholders. Originally, in his consideration of the plan in January and February, 1955, he also anticipated that the price of the common stock would increase after consummation of the plan to some premium over the increased asset value resulting from the elimination of dividend arrears under the exchange offer, and that this increase would be reflected in an increase in the market price of the new preferred stock. However, when he testified he explained that he had changed this view and no longer anticipated that the Alleghany common stock would sell at a premium over its asset value, but that he instead anticipated that it would, like other investment companies, sell at some discount from asset value, probably between 25% and 40%. He was of the opinion that the market price of the common stock prior to the effective date of the exchange offer largely reflected the benefits anticipated from the increase in asset value as a result of the exchange offer, so that he did not contemplate a further increase in the price of that stock by virtue of the consummation of the plan.[24]

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[24] Wallace testified that Alleghany's officers, including Young and Kirby, anticipated that most of the benefits of the plan to the common stock, including the increased asset value, would be reflected in the market price of the common stock prior to the date on which the exchange ratio was fixed, although it was recognized that there might be some slight increase as a result of the plan after that date. He further stated that they did not anticipate that the approximately $3.80 increase in asset value which results from the exchange offer would be accompanied by a similar increase in market value, but rather that the common stock of Alleghany, like that of other closed-end investment companies, would sell at some discount from its asset value, although no one was certain of the extent of that discount. In this connection,

In brief, the foregoing shows the undisputed highly speculative and volatile nature of the new preferred stock with the difficulties inherent in its evaluation because of its character as a right to purchase, which renders it inappropriate in the capital structure of an investment company such as Alleghany. The very experts introduced in support of the plan differed sharply as to the ultimate value of the new preferred stock, the determinant here of the question of fairness, producing a record which does not permit our making the requisite findings as to fairness. As we have seen, one of the expert witnesses believed that the new preferred stock receivable under the exchange offer for each share of old preferred stock would attain a value in excess of $400 after final consummation of the plan. The other expert witness originally expressed a similar judgment but when he appeared at the hearings stated that he had changed his opinion. This difference and change of opinion as to value not only demonstrates the unclear and conflicting nature of the record with respect to whether the plan is within the range of fairness, but it also shows the complex problems which would face an ordinary investor seeking to appraise Alleghany's securities.

It has been contended that any increases in the value of the new preferred stock which might occur after final consummation of the plan would not be at the expense of the common stockholder but would be generated in the market place, with both the preferred and common stockholders benefiting there-

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Wallace pointed out that the price of the common stock had risen to a point where it was no longer a very low-priced stock and that the rise in value of such holdings as IDS which was anticipated when the stock was selling at a premium had now been realized.

from. However we cannot accept this argument as supporting the fairness of the exchange offer. This argument ignores the fact that it was implicit in the formulation and adoption of the exchange offer that most if not all of the benefits to be realized from the plan would be reflected in the price of Alleghany's common stock on the date as of which the conversion ratio was to be fixed. However, as we have seen, the record contains substantial evidence indicating that this expectation was not realized, with the result that the new preferred stock receivable under the exchange offer for each share of old preferred stock would attain a market value after consummation of the exchange far in excess of what might be considered within the permissible range of fairness. Furthermore, the argument emphasizes the highly speculative nature of the right to purchase common stock, which is the essence of the new security, and the inappropriateness of issuing an order of exemption pursuant to Section 6 (c) as consistent with the protection of investors.

CONCLUSION

We have determined that it would be inappropriate to declare that no approval or other action on our part is now required under the Act with respect to the transactions involved in the exchange offer. We have also found that the new preferred stock falls within the prohibition of Section 18 (d) of the Act, and that on the basis of the record before us we cannot find that the exchange offer falls within the range of fairness. Under all the circumstances, we conclude that an exemption is not necessary or appropriate in the public interest or consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Act. In reaching this conclusion we are mindful of the position in which the preferred

stockholders find themselves by virtue of the restrictions on trading that have been imposed. However, such restrictions were not the consequence of any action by us and they cannot alter the nature of our responsibility to apply the standards of the Act. Accordingly, we shall deny the application.

To whatever extent the proposed findings and exceptions involve issues which are relevant and material to the decision of this case we have by our detailed Findings and Opinion herein already ruled upon them. We hereby expressly approve these requested findings and sustain those exceptions to the extent that they are in accord with the views set forth herein, and we expressly overrule those exceptions and disapprove those proposed findings to the extent that they are inconsistent with such views.

An appropriate order will issue.

By the Commission (Chairman Armstrong and Commissioners Orrick, Hastings and Sargent), Commissioner Patterson filing a dissenting opinion (attached).

ORVAL L. DUBOIS, *Secretary.*

Commissioner PATTERSON, *Dissenting*:

I would grant an exemption with respect to the exchange offer.[1]

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[1] I would condition the exemption to require Alleghany to make an offer of rescission in compliance with the provisions of the Securities Act of 1933. Alleghany has not registered the new preferred stock under that Act, nor delivered a prospectus to security holders, claiming the exemption provided in Section 3 (a) (6) of that statute for securities issued by a common or contract carrier, the issuance of which is subject to the provisions of Section 20 (a) of the Interstate Commerce Act, as amended." However, it has been judicially determined that Alleghany was not subject to the provisions of the latter section.

In my opinion the new preferred stock is exempt from the provisions of Section 18 of the Act. Section 18 (c) (2) exempts from the provisions of Section 18 senior securities issued by a closed-end company in connection with a refunding of the type here presented. Section 18 (g) defines a senior security as "* * * any stock of a class having priority over any other class as to distribution of assets or payment of dividends * * *" The new preferred stock carries with it a priority over the common stock as to distribution of assets and payment of dividends and therefore comes within the specific statutory definition of a senior security.

I recognize that certain difficulties of evaluation and appraisal are presented by the evidence of record. However, it is my opinion on the basis of the record that the exchange offer falls within the permissible range of fairness. Determinations as to fairness need not and usually cannot be based on precise values and fairness may be found to exist within a range of values.[2]

Alleghany's old preferred stock had been outstanding for many years. As of May 1, 1955, the old preferred stock could be redeemed only by payment in cash of the redemption price of $105 per share, plus unpaid dividend arrears of $132, or a total of $237. Under the exchange offer each share of the $100 par value old preferred stock is exchangeable at the option of the holder for ten shares of 6% Convertible Preferred Stock, $10 par value. The new preferred is entitled in the event of voluntary liquidation or redemption to 105% of par value or $10.50, and in the

[2] See, e. g., *In the matter of The American Superpower Corporation, et al.*, Investment Company Act Release No. 1758 (May 19, 1952); *In the matter of The Standard Investing Corporation, et al.*, 8 S. E. C. 1019 (1941).

event of involuntary liquidation to par value, plus accrued dividends in each case. The new preferred stock is not redeemable prior to May 1, 1970, but is convertible at any time. The new preferred stock will be entitled to a cumulative dividend of 60 cents per share per year, or $6.00 on the ten shares received in exchange for each share of the old preferred.

The new preferred stock is convertible into shares of common stock upon the payment of $3.75 per share of common stock. The number of common shares into which each new preferred share may be converted was to be fixed as of May 25, 1955, so that as of that date the market price of the common stock securable upon conversion of ten shares of the new preferred stock, less the $3.75 per share conversion payment, would be equal to approximately $237, the redemption price.

While the annual dividend preference on the new stock is slightly higher than the $5.50 dividend on the old stock, this is of little significance, since no return is being offered on the unpaid dividend arrears and the record indicates that the new stock is of such quality that but for its conversion feature its market value would be less than its par value.

In order that the new preferred stock would have a value sufficient to induce the old preferred stockholders to relinquish voluntarily their relatively well secured senior claim and to accept the exchange, and because of the speculative character of the conversion privilege, it was necessary to offer a premium over the redemption claim of $237, with this premium to be realized as a result of the 15-year non-callable feature. Recognizing the advantages accruing to the common stockholders from the exchange offer and the necessity for providing sufficient inducement to the preferred stockholders to accept the exchange, I do not believe that the amount of the premium offered the

preferred stockholders under the exchange offer is so great as to place it outside the permissible limits of fairness. I think that the market prices of the Alleghany common stock as of May 25, 1955, largely, if not entirely, reflected the anticipated benefits from the exchange offer and that actual consummation of the offer would not have the effect of increasing the price of the common stock beyond such limits.

Moreover, it should be noted that the anticipated premium on the new preferred stock is not one which can be immediately realized by all of the old preferred stockholders because the record indicates that if disposition were attempted of any substantial number of new shares immediately upon the consummation of the exchange offer, the premium would certainly narrow and probably disappear. Consequently, preferred stockholders who accepted the exchange offer would have to retain their investments for varying periods of time during which they would be exposed to fluctuations in the price of the underlying common stock.

In addition, in considering the fairness of this voluntary exchange offer, weight may appropriately be given to the overwhelming approval of the offer by all classes of stockholders of Alleghany.

APPENDIX A

ALLEGHANY CORPORATION

Statement of income, year ended December 31, 1955, with comparative figures for 1954

	1955	1954
Income (exclusive of security transactions):		
Dividends	$1,593,000	$702,529
Interest earned on investments	342,714	246,796
Other interest and miscellaneous	575,665	726,790
Total income	2,511,379	1,676,115
Expenses:		
Interest on debentures and bank loans	874,354	881,061
Amortization of debt expenses	9,387	13,434
Administrative and general expenses	1,143,512	829,098
Advances and expenses re Missouri Pacific Railroad Company reorganization	92,405	57,769
Total expenses	2,119,658	1,781,362
Income (loss) (exclusive of profit and loss on security transactions) before provision for Federal taxes on income	391,721	(105,247)
Provision for Federal taxes on income (including $40,000 for prior years)	75,000	
Net income (loss) (exclusive of profit and loss on security transactions) transferred to earned surplus (deficit)	316,721	(105,247)

Statement of profit and loss on security transactions

Net gain on sales of securities	$1,989,172	$3,812,645
Net gain on joint ventures		466,103
Net gain on security transactions transferred to earned surplus (deficit)	1,989,172	4,278,748

UNITED STATES OF AMERICA

before the

SECURITIES AND EXCHANGE COMMISSION

November 30, 1956

IN THE MATTER OF ALLEGHANY CORPORATION

(Files Nos. 812-987, 812-988, 812-998)

(Investment Company Act of 1940—Section 6 (c))

ORDER DENYING APPLICATION

Alleghany Corporation ("Alleghany"), a registered investment company, certain holders of its 5½% Cumulative Preferred Stock, Series A, and certain holders of its common stock and warrants, having filed separate applications for a declaration that no approval or other action of the Commission is required under the Investment Company Act of 1940 with respect to the transactions involved in the exchange of said 5½% Cumulative Preferred Stock for 6% Convertible Preferred Stock of Alleghany, or, in the alternative, for an order pursuant to Section 6 (c) of said Act exempting said transactions from the provisions thereof.

Proceedings on said applications having been consolidated, public hearings having been held after appropriate notice, proposed findings and briefs having been filed, the Division of Corporate Regulation having filed Proposed Findings and Conclusions, and exceptions thereto having been filed; and

The Commission having this day entered its Findings and Opinion herein; on the basis of such Findings and Opinion

IT IS ORDERED that the aforesaid applications be, and they hereby are, denied.

By the Commission.

ORVAL L. DUBOIS, *Secretary*.

APPENDIX C

(Investment Company Act Release No. 1990)

UNITED STATES OF AMERICA

before the

SECURITIES AND EXCHANGE COMMISSION

July 7, 1954

IN THE MATTER OF ALLEGHANY CORPORATION

(File No. 811–338)

(Investment Company Act of 1940)

NOTICE OF AND ORDER FOR HEARING

Part I

According to information contained in the files of this Commission, it appears that:

1. On the 1st day of November, 1940, Alleghany Corporation, ("Alleghany"), a company organized under the laws of the State of Maryland, filed with this Commission its notification of registration under the Investment Company Act of 1940 ("the 1940 Act") as a closed-end, non-diversified, management investment company.

2. On June 5, 1945 the Interstate Commerce Commission ("ICC"), in proceedings initiated by Alleghany (Chesapeake & Ohio Railway Purchase etc., Finance Docket No. 14692), entered its order providing, among other things:

> "*It is further ordered,* That acquisition by the Alleghany Corporation of control, through

ownership of stock, of The Chesapeake and Ohio Railway Company, The New York, Chicago and St. Louis Railroad Company, and the Pere Marquette Railway Company, and their subsidiaries and affiliates, be, and it is hereby, approved and authorized: Provided, however, that this authorization and approval are granted subject to the express conditions numbered (1), (2), and (3), relative to the depositing of stocks with independent voting trustees and to the elimination of interlocking directors, set forth in said report.

"*It is further ordered,* That unless and until otherwise ordered by this Commission said Alleghany Corporation shall be considered as a carrier subject to the provisions of Section 20 (1) to (10), inclusive, and Section 20a (2) to (11), inclusive, of the Interstate Commerce Act to the same extent that those provisions are applicable to the Chesapeake and Ohio Railway Company and its carrier subsidiaries and affiliates; * * *"

3. On October 4, 1945 this Commission entered its Findings, Opinion and Order in these proceedings pursuant to Section 8 (f) of the 1940 Act in which the Commission found, on the basis of the June 5, 1945 order of ICC and upon review of the provisions of the Interstate Commerce Act to which Alleghany was declared subject by said order of the ICC, that Alleghany was subject to regulation under the Interstate Commerce Act, and therefore by virtue of Section 3 (c) (9) of the 1940 Act excepted from the definition of an investment company, and ordered as follows:

It is hereby declared that Alleghany Corporation has ceased to be and is not now an investment company within the meaning of the Investment Company Act of 1940; and

It is ordered that the registration of Alleghany Corporation under the Investment Com-

pany Act of 1940 shall forthwith cease to be in effect, provided, however, that if in the future Alleghany Corporation ceases to be subject to regulation under the Interstate Commerce Act as set forth in such Findings and Opinion, this order may be revoked, suspended or modified after appropriate notice and opportunity for hearing.

4. On June 22, 1954, the ICC entered an order in Finance Docket No. 14692 reciting and ordering, *inter alia*, as follows:

> *It further appearing,* That counsel for Alleghany Corporation has stated to the Commission that Alleghany Corporation and its affiliates have divested themselves of control of the Chesapeake and Ohio Railway Company and the Vice President and General Counsel of the Chesapeake and Ohio Railway Company had advised the Commission of various steps taken to effectuate such divestments of control.
>
> *And it further appearing,* That Alleghany does not propose to exercise further the authority granted by said order of June 5, 1945, and that it should no longer be considered a carrier for the purposes of Section 20 (1) to (10), inclusive, or Section 20a (2) to (11), inclusive.
>
> It is ordered, That said Alleghany Corporation shall, on or before July 15, 1954, show cause why said order of June 5, 1945, so far as it applies to Alleghany Corporation, should not be vacated and set aside and be no longer of any force and effect.

5. On June 29, 1954, Alleghany filed its response to said order of the ICC dated June 22, 1954, in which Alleghany stated that "* * * it has no objection, but agrees, to the entry of an order, forthwith, formally terminating the authority granted to Alleghany by the Commission's Order of June 5, 1945, to control The Chesapeake and Ohio Railway Company," and re-

quested an extension of time until October 1, 1954, to respond to that portion of the ICC order which contemplates that Alleghany should be declared to be no longer subject to certain provisions of the Interstate Commerce Act. In support of its request for extension of time Alleghany stated, in part, "Requiring Alleghany now to assume non-carrier status would involve numerous changes, and would be unnecessarily burdensome were Alleghany to be shortly thereafter required to resume carrier status."

On July 1, 1954, the ICC entered its order denying the requested extension of time.

6. As shown by its balance sheet of December 31, 1953, Alleghany had outstanding the following securities: $7,872,000 principal amount of 5% Sinking Fund Debentures, due 1962; $14,000,000 principal amount of Notes Payable to Banks, due 1954 to 1956; $2,067,600 stated value of $4 Prior Preferred Convertible Stock; $13,674,400 par value of 5½% Preferred Stock and $4,637,797 par value of common stock.

Additionally the balance sheet discloses that Alleghany's Paid-in Surplus was $107,118,632 and that it had an Earned Surplus deficit of $92,840,889. At December 31, 1953, dividend arrears on the 5½% Preferred Stock amounted to $17,047,419.

7. The total assets of Alleghany as of December 31, 1953, were stated at $56,850,032, of which $42,066,001 represented investments stated approximately at market value. Other assets included $9,233,457 of notes receivable. Its investments included securities of twenty-eight different companies engaged in various businesses including steel, oil, gas, aircraft, utility, transportation and manufacturing. Its largest single investment was in a controlling block of stock of Investors Diversified Services, Inc., a registered invest-

ment company, which in turn controls and manages other registered investment companies. Investments in transportation companies were stated at a market value of $7,892,709.

8. Since the end of 1953 Alleghany has disposed of its investment in the common stock of The Chesapeake and Ohio Railway Company. Its other investments in transportation companies as of December 31, 1953, were stated at a market value of approximately $4,419,420.

9. Alleghany filed with the Commission a proxy statement dated April 8, 1954, containing, inter alia, the following representation:

ALLEGHANY'S ACQUISITION PROGRAM

> Alleghany, which has sold all of its Chesapeake and Ohio Railway Company stock, intends to acquire Central [The New York Central Railroad Company] stock from time to time. It holds short-term notes of Mr. Murchison [Clinton W. Murchison] and Mr. Richardson [Sid W. Richardson] totalling $7,500,000 due September 15, 1954 and bearing 4½% interest, the proceeds of which together with temporary borrowings of $5,000,000 from Mr. Kirby [Allan P. Kirby] and $7,500,000 from a group of banks, were applied by Mr. Murchison and Mr. Richardson to their purchases of their 800,000 shares of Central. They have the right to require Alleghany, at their several options, to purchase from them up to a total of 400,000 of such shares, but only between July 15 and September 15, 1954, at $25 per share. If they exercise in whole or in part such options covering 200,000 of their shares, they must also contribute an equal number of shares, which, with the shares so purchased by Alleghany, must be subjected to joint venture agreements with Alleghany under which, in effect, Alleghany will

provide the capital, will be entitled to half of all income and profits and will be guaranteed by such other parties against losses. Mr. Richardson also has the right to require Mr. Kirby to purchase from him 200,000 additional shares of Central stock at $25 per share between June 1–10 and July 11–15, 1954.

There is no understanding with or determination by Mr. Murchison or Mr. Richardson as to whether either or both will exercise any or all such rights to require purchase of these shares of Central stock presently owned by them. If Alleghany shall not acquire interests in Central stock through the exercise of these options by Mr. Murchison and Mr. Richardson, it intends otherwise to acquire stock of Central with the proceeds from the payment of such notes it holds from Mr. Murchison and Mr. Richardson, or from other funds available to it. This, of course, does not constitute a representation by Alleghany that it will purchase in the market any given amount of Central stock at any given time or price.

Part II

It appearing to the Commission, on the basis of the facts set forth in Part I hereof that substantial questions exist (a) whether Alleghany is an investment company within the meaning of Section 3 of the 1940 Act and subject to the provisions of Section 7 thereof; and (b) whether Alleghany is, or may be, no longer subject to regulation under the Interstate Commerce Act within the meaning of Section 3 (c) (9) of the 1940 Act and this Commission's order of October 4, 1945; (c) whether this Commission's order of October 4, 1945 should be revoked, suspended or modified in accordance with the policy and provisions of the 1940 Act for the protection of investors and in the public interests; and (d) whether any proposed acts or trans-

actions require that Alleghany register as an investment company and that further proceedings be had before the Commission.

Part III

WHEREFORE IT IS ORDERED that a hearing under the applicable provisions of the 1940 Act and the Rules of the Commission be held on the 27th day of July 1954, at 10:00 a. m. at the offices of the Securities and Exchange Commission, 425 Second Street NW., Washington 25, D. C. with respect to the following specified matters and questions, without prejudice, however, to the specification of additional issues which may be present in these proceedings:

1. Whether or not Alleghany is an investment company within the meaning of Section 3 of the 1940 Act and subject to the provisions of Section 7 thereof.

2. Whether or not Alleghany is subject to regulation under the Interstate Commerce Act within the meaning of Section 3 (c) (9) of the 1940 Act.

3. Whether or not the Commission's order of October 4, 1945 entered in these proceedings should be revoked, suspended or modified and what terms and conditions, if any, should be imposed in connection with such revocation, suspension or modification.

4. Whether or not, with respect to any acts or transactions in which Alleghany, or any affiliated person of Alleghany, or any affiliate of such a person, is engaged or proposes to engage, including those referred to in paragraph 9 of Part I hereof, the 1940 Act requires that Alleghany shall have registered as an investment company prior to their consummation, and that appropriate application shall have been filed with and granted by the Commission.

IT IS FURTHER ORDERED that William W. Swift, or any officer or officers of the Commission designated by

it for that purpose shall preside at the hearing, and any officer or officers so designated to preside at any such hearing is hereby authorized to exercise all of the powers granted to the Commission under Sections 41 and 42 (b) of the Investment Company Act of 1940 and to hearing officers under the Commission's Rules of Practice.

NOTICE OF SUCH HEARING is hereby given to the Interstate Commerce Commission and Alleghany. Notice is also given to any other person or persons whose participation in such proceedings may be necessary or appropriate in the public interest or for the protection of investors. Any answer or pleading by Alleghany with respect to the factual allegations contained in Part I or the issues herein shall be filed with the Secretary of the Commission on or before July 20, 1954. Any other person desiring to be heard in said proceeding should file with the hearing officer or the Secretary of the Commission, on or before July 26, 1954, his application therefor as provided by Rule XVII of the Rules of Practice of the Commission, setting forth therein any of the issues of law or fact which he desires to controvert and any additional issues he deems raised by the aforesaid applications.

By the Commission.

ORVAL L. DUBOIS, *Secretary.*

APENDIX D

(Investment Company Act Release No. 2022)

UNITED STATES OF AMERICA

before the

SECURITIES AND EXCHANGE COMMISSION

October 18, 1954

IN THE MATTER OF ALLEGHANY CORPORATION

(File No. 811–338)

(Investment Company Act of 1940)

ORDER POSTPONING HEARING

On July 7, 1954 this Commission issued its Notice of and Order for Hearing in these proceedings (Investment Company Act Release No. 1990) ordering that hearings herein be held July 27, 1954. On July 19, 1954 Alleghany Corporation filed a Motion to Postpone said hearings until a date to be subsequently determined, and pursuant to stipulations between Alleghany and the Commission said hearings were postponed from time to time until October 19, 1954.

Alleghany having renewed its Motion to Postpone, on October 15, 1954, it was further stipulated between Alleghany and the Commission that the hearings in these proceedings be further postponed subject to call of the Trial Examiner but with not less than 15 days' notice to Alleghany; provided, however, that if the Interstate Commerce Commission, before call of the Trial Examiner, revokes, modifies or suspends its

order dated June 5, 1945, entered in Finance Docket 14692, in such manner as to relieve Alleghany from compliance with certain provisions of the Interstate Commerce Act specified in said order, then until the conclusion of the hearings herein Alleghany will not, without first obtaining the approval of this Commission, engage in any act or consummate any transactions which, if Alleghany were registered under the Investment Company Act of 1940, would by the terms of that Act either be prohibited or require an order of this Commission exempting or approving such transactions before their consummation.

The Commission being of the opinion, on the basis of the stipulation of October 14, 1954, above recited, that the Motion to Postpone the hearings in these proceedings may appropriately be granted in the public interest and the interest of investors:

IT IS HEREBY ORDERED that the Motion to Postpone the hearings ordered to be held on October 19, 1954 in these proceedings be, and the same hereby is granted and said hearings be and the same are hereby postponed subject to call of the Trial Examiner but with not less than 15 days' notice to Alleghany.

By the Commission.

ORVAL L. DUBOIS, *Secretary*.

APPENDIX E

Before the

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C.

IN THE MATTER OF ALLEGHANY CORPORATION

(File No. 811-338)

(Investment Company Act of 1940)

MOTION TO POSTPONE HEARING

* * * * *

Alleghany respectfully requests that such hearing be postponed pending action by the Interstate Commerce Commission on its Order to Show Cause dated June 22, 1954, in Finance Docket No. 14692. In support of this motion, Alleghany shows the following:

* * * * *

4. The Interstate Commerce Commission has issued an Order to Show Cause why its Order of June 5, 1945, declaring Alleghany subject to the Interstate Commerce Act, "should not be vacated and set aside and be no longer of any force and effect." A copy of Alleghany's Response to this Order to Show Cause is attached hereto. As shown therein, Alleghany now controls the New York Central Railroad Company and all of its affiliated and subsidiary carriers in the same manner and to the same extent that it controlled The Chesapeake & Ohio Railway and its affiliated and subsidiary carriers. The Chairman of Alleghany is Chairman of Central. The Board of Central is that

nominated by Alleghany. This Board since its election has installed a new President, Secretary and Vice President-Law. Alleghany believes on the basis of this Response and the facts stated therein the ICC will continue to subject Alleghany to regulation under the Interstate Commerce Act. However, should the ICC vacate its Order, then the hearing in this proceeding would be unnecessary since Alleghany would revert to the jurisdiction of this Commission under the 1940 Act.

* * * * *

WHEREFORE, Alleghany respectfully requests the Commission postpone the date of the hearing in the above-entitled matter, now scheduled for July 27, to a date not less than ten days after the Interstate Commerce Commission issues its order determining whether or not to continue to subject Alleghany to regulation under the Interstate Commerce Act as provided in Section 5 (3).

Respectfully submitted,

WHEELER & WHEELER,
By Edward K. Wheeler.
EDWARD K. WHEELER.

JULY 19, 1954.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 36.

ALLEGHANY CORPORATION, *et al.*,
Appellants,

v.

BRESWICK & CO., RANDOLPH PHILLIPS and MYRON NEISLOSS, as common stockholders of Alleghany Corporation, individually and on behalf of all other common stockholders of Alleghany Corporation similarly situated,
Appellees.

No. 114.

INTERSTATE COMMERCE COMMISSION,
Appellant,

v.

BRESWICK & CO., *et al.*,
Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK.

BRIEF FOR APPELLEES.

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Dated: January 15, 1957.

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